




THE BULGARIAN ECONOMY

IN THE FIRST QUARTER OF 2003

REPORT BY
**THE CENTER
FOR ECONOMIC
DEVELOPMENT**



The Center for Economic Development (CED) is a Bulgarian non-governmental research institute in the area of economic policy, established in 1997. Its goal is to support the economic development of Bulgaria through encouragement of public debate on economic issues and development of economic policy options.

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1408 Sofia, 1 Balsha St., bl. 9
e-mail: aeconomy@ced.bg


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ABBREVIATIONS USED

| | |
|------|---|
| AD | JOINT STOCK COMPANY |
| ASME | AGENCY FOR SMALL AND MEDIUM-SIZED ENTERPRISES |
| BCCI | BULGARIAN CHAMBER OF COMMERCE AND INDUSTRY |
| BDJ | BULGARIAN RAILWAY COMPANY |
| BDU | BULGARIAN DOCTORS UNION |
| BIA | BULGARIAN INDUSTRIAL ASSOCIATION |
| BNB | BULGARIAN NATIONAL BANK |
| BRS | BULGARIAN RIVER SHIPPING |
| BSE | BULGARIAN STOCK EXCHANGE |
| BTC | BULGARIAN TELECOMMUNICATIONS COMPANY |
| CITA | CORPORATE INCOME TAXATION ACT |
| CoM | COUNCIL OF MINSISTERS |
| CPC | COMMISSION FOR PROTECTION OF COMPETITION |
| DTA | DOUBLE TAXATION AVOIDANCE |
| EA | EMPLOYMENT AGENCY |
| EAD | SINGLE OWNER JOINT STOCK COMPANY |
| EC | EUROPEAN COMMUNITY |
| EIA | ENVIRONMENTAL IMPACT ASSESSMENT |
| ERC | ENERGY REGULATORY COMMISSION |
| EU | EUROPEAN UNION |
| FS | FREE SOFTWARE |
| FSC | FINANCIAL SUPERVISION COMMISSION |
| GDP | GROSS DOMESTIC PRODUCT |
| GS | GOVERNMENT SECURITIES |
| GVA | GROSS VALUE ADDED |
| HPP | HYDRO POWER PLANT |
| ICT | INFORMATION AND COMMUNICATIONS TECHNOLOGY |
| IME | INSTITUTE FOR MARKET ECONOMY |
| IMF | INTERNATIONAL MONETARY FUND |
| IS | INFORMATION SYSTEM |
| MEW | MINISTRY OF ENVIRONMENT AND WATER |
| MLSP | MINISTRY OF LABOR AND SOCIAL POLICY |
| MNB | MARITIME NAVIGATION BULGARE |
| MoE | MINISTRY OF ECONOMY |
| MoF | MINISTRY OF FINANCE |
| MTC | MINISTRY OF TRANSPORT AND COMMUNICATIONS |
| NFA | NATIONAL FRAMEWORK AGREEMENT |
| NGO | NON-GOVERNMENT ORGANIZATION |
| NHIF | NATIONAL HEALTH INSURANCE FUND |
| NPP | NUCLEAR POWER PLANT |
| NSI | NATIONAL STATISTICAL INSTITUTE |
| NSSI | NATIONAL SOCIAL SECURITY INSTITUTE |
| OECD | ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT |
| PA | PRIVATIZATION AGENCY |
| PIC | PENSION INSURANCE COMPANY |
| PPCA | PRIVATIZATION AND POST-PRIVATIZATION CONTROL ACT |
| RHIF | REGIONAL HEALTH INSURANCE FUND |
| RIE | REGIONAL INSPECTORATE OF ENVIRONMENT |
| SME | SMALL AND MEDIUM-SIZED ENTERPRISES |
| UDB | UNION OF DENTISTS IN BULGARIA |
| UN | UNITED NATIONS |
| UPF | UNIVERSAL PENSION FUND |
| VAT | VALUE ADDED TAX |
| VATA | VAT ACT |

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Continuing GDP growth gives grounds for a positive general assessment of Bulgarian economic development in the first quarter of 2003. A number of sectors and areas like industry, tourism, exports, banking system, and capital market, register positive dynamics. Good macro-economic indicators for inflation, labor market, and incomes add to the conclusion about preserved economic stability and continuing growth in the first quarter of 2003.

At the same time, good indicators' dynamics does not necessarily imply sustainability, and the need to substantially improve some indicators persists. Efficiency of implemented policy remains a topical and acute issue. Examples of successfully implemented specific government economic policy are reduced to areas like social security, employment, development of environmental regulations, support to agricultural producers. Privatization, foreign investments, healthcare reform and judiciary system policies, as well as sector policies in transport and in high technology and communications can be given neutral (no positive development) or negative assessment. The negotiation process with the European Union registers delay.

On the whole, the precarious good indicators - economic policy balance confirms the neutral assessment of the business climate and is manifested in contradictory evaluations of the individual elements of Bulgarian business environment.

Business climate in Bulgaria is evaluated employing a summarized estimate of the indicator by the representatives of some 400 interviewed enterprises. The latest survey was conducted in early April. The **Estat index of business climate** integrated estimate for the first quarter of 2003 is -0.61 (compared to -2.55 for the last quarter of 2002) and remains within the neutral portion of the scale. The index value is very close to that registered in April last year, which may well indicate a seasonal character of entrepreneurs' assessments. Business environment remains unstable. Optimistic expectations about

the next months do not have effect on investment attitudes and on managers' realistic assessment of their opportunities in a competitive business environment. The tendency to take risks to expand the business registers a notable downward trend. Despite the shortage of financial resources, most of the interviewed state that they would not compensate this deficit by taking a bank loan. Annual closing of accounts and administrative problems increase critical assessments and the tendency to use unregulated methods to overcome barriers. Disapproval of government legislative initiatives registers a notable upward trend.

A comparison with the first quarter of 2002 - the period of first surveys, reveals a more definite positive trend in the opinion of the business about tax environment. Despite that, entrepreneurs continue to point out as their major problem the difficulties in the start up of new business. The business preserves its rather positive attitude towards harmonization of Bulgarian with European legislation and expectations for corresponding improvement of the business environment persist, but nevertheless there is a serious need of more active involvement of entrepreneurs in the harmonization process and of higher awareness about the effects of requirements towards the business. Confidence in the banking system increases. But on the whole, entrepreneurs think that government's business promotion policy is not so well-directed and efficient. Businessmen's opinion about government legislative initiative remains negative. Some positive change is observed in the assessments of legislative implementation, but on the whole businessmen are of the opinion that legislative activity generates uncertainty and inability to plan one's business. It should be noted again that assessments about the judiciary system confirm the existence of serious problems in this area. The propensity of the business to pay extra money to quickly solve administrative problems persists, that is, tolerance of corruption remains high.

In the first quarter of 2003 **NSI's general business**

climate indicator registers a drop compared to the previous quarter. On the other hand, industrial business climate indicators are at lower levels compared to the first quarter of 2002. The business climate indicator in construction is at rather high levels. Business climate indicators in retail trade are at higher levels compared to the first quarter of 2002 and move around their 2002 end levels. According to NSI's business surveys again, business climate dynamics in the services sector seems most unfavorable in the first quarter of 2002.

In the first quarter of 2003 **GDP growth** taken on an annual basis is expected to exceed the growth in the first quarter of 2002 (3.4 per cent). Expectations are supported by the notably higher growth on an annual basis of monthly industry sales (particularly the growth of export sales in February and March - 37 and 64.7 per cent, accordingly) and trade sales, by industrial output growth, and by data about the export and import of goods, which are considerably higher compared to the first quarter of 2002 and indicate intensified demand and supply. In terms of **inflation**, consumer price movement in the first quarter remains negligible per se, as well as compared to the price movement per industrial producer, which is explainable by the imports competition on the industrial consumer goods market and by the modest share of local industrial goods in the consumer basket. "From the dark into the light" movements are outlined on the **labor market**, which is proven by the notable decrease in the number of registered unemployed and the significant increase in the number of the employed. But a parallel flow "from the light into the dark" is probably observed too, because the difference between the number of registered unemployed and people who define themselves as unemployed registered abrupt increase compared to the end of 2002.

The first quarter of 2003 is characterized by rather good execution of the **budget**, with consolidated budget revenues for the first three months amounting to BGN 3 220.6 m, or slightly above 24 per cent

of annual program revenues, and expenditures amounting to BGN 3 109.8 m, or 22.8 per cent of annual program expenditures.

At the end of the first quarter of 2003, total **state and state-guaranteed debt** amounted to BGN 17 560 m (recalculated at BNB's exchange rates of the Bulgarian Lev as of 31 March 2003), accounting for 49.8 per cent of GDP. Total debt registered a decrease of BGN 620 m compared to the end of 2002. But in USD equivalent terms, total state and state guaranteed debt increased by USD 137 m in the period end of 2002 - end of March 2003 (from USD 9 645 m to USD 9 782 m).

In the period end of December 2002 - end of March 2003, total **foreign debt** registered an increase of USD 45.7 m. But in BGN terms, Euro's appreciation resulted in decrease of the debt by BGN 677.5 m. As of end of March 2003 total foreign debt amounted to USD 8 506 m, or BGN 15 270 m., whereas total **domestic debt** amounted to BGN 2 290.6 m, registering an increase of BGN 178.8 m, compared to the end of 2002.

In the first quarter of 2003 the pace of **privatization** in the state sector remains rather unsatisfactory. Only 12 transactions for sale of companies with majority (more than 50 per cent) state interest and 7 for detached parts were made. Notably higher non-fulfillment of the plan was registered in terms of the sale of minority blocks of shares - only 25 transactions. Thus approximately a monthly share of PA's Annual Privatization Plan was fulfilled in the first three months of 2003. Government efforts were focused on completing the privatization procedures for Bulgartabac Holding AD and BTC EAD. The Constitutional Court repealed proposed amendments to PPCA which were aimed at eliminating the opportunity for judicial review of 15 privatization transactions. The sale of the two companies was never completed. In the beginning of March the Government undertook before the World Bank to privatize by the end of 2003 Bulgartabac Holding AD, DSK Bank, Maritime Navigation Bulgare,

Bulgarian River Shipping, and Balkancar Holding. The privatization of 20 small HPPs and sale by the end of September of not less than half of the remaining state-owned small and medium-sized enterprises are added to government commitments. Anticipated finalization of the privatization of BTC EAD by the end of 2003 is also stated in the letter to the World Bank. Government commitments are a condition for receiving the second tranche of the PAL loan. In the area of privatization via the stock exchange, PA's Supervisory Board and CoM approved a List of commercial companies with state interest in their capital for which privatization against payment in non-cash instruments is allowed. Some of the approved amendments to PPCA envisage official entry of companies, for which a decision is made to sell shares therefrom by way of public offering, in the register of the Financial Supervision Commission. These amendments are regarded as favorable for capital market development.

The first quarter of 2003 was characterized by active public debate on the problems of **small and medium-sized enterprises**, which indicates certain governmental effort to maintain the dialogue with the Bulgarian small and medium-sized business. That is proved by the National Forum on the Problems of Small and Medium-Sized Enterprises, organized by the Agency for Small and Medium-Sized Enterprises, and by two events organized by the Bulgarian Industrial Association in March 2003. At the forum organized by ASME the government stated for the first time that a portion of the credit guarantees will not be undertaken by a guarantee fund, although the Small and Medium-Sized Enterprises Act regulates the set up of such a fund. The draft law for amendment of the Small and Medium-Sized Enterprises Act introduced in parliament on 25 February 2003 provides for set up of a Guarantee Fund in Support of the Small and Medium-Sized Business with state interest of 51 per cent, however at this stage the government desists from fulfillment of commitments in this area.

First quarter data about Bulgarian **foreign trade** are a

positive surprise against the background of European economic recession and negligible US economic growth. Exported goods amounted to USD 1709.2 m, registering a growth of 42.3 per cent compared to the same period of 2002. Even if the exchange rate effect is neglected, growth remains notable – 19.2 per cent (in BGN). Imports (CIF) amount to USD 2190 m, registering an increase of 39.1 per cent in USD and 16.4 per cent in BGN. They register smaller growth against exports, but that is not enough to decrease the negative balance. Registered deficit amounts to around USD 500 m (export FOB - import CIF), and remains some 35 per cent higher compared to the first quarter of 2002, but around the average quarterly level for the previous year. Alongside with traditional partners (EU, OECD countries and neighboring Balkan states), certain more or less forgotten markets like China, Egypt and Brazil account for increasingly higher share in the geographic structure of trade.

In the first quarter of 2003 the volume of **foreign investments** in Bulgaria (USD 181.5 m) registered an increase by USD 55 m (or 43.7 per cent) compared to the first quarter of 2002. But the structure of foreign direct investments should also be analyzed – attracted funds from non-residents and reserves of Bulgarian companies account for 56.6 per cent (or USD 102.7 m) of total FDI, and the remaining USD 78.8 m come from operations with intercompany loans. A possible conclusion is that Bulgarian economy remains in acute shortage of sizable green field investments and of sustainable inputs by strategic investors.

The beginning of 2003 was characterized by new preparative efforts of government authorities to place the Bulgarian **energy sector** on a market footing. The ultimate result of these actions will contribute for improved competitiveness of energy-intensive productions, more favorable business climate in the energy sector, and facilitated adaptation of Bulgarian economic actors to the European market. The passing of an act regulating the obligations to maintain oil and oil product reserves will facilitate the negotiation process for Bulgaria's accession to the

EU. The ambiguous situation around the validity of Bulgaria's commitment to close down units 3 and 4 of Kozloduy NPP in 2006 will have an opposite effect.

Oil prices remained unstable, reaching record-breaking levels for the last decade. Their upward trend was felt in Bulgaria in the higher prices of oil products and natural gas and had unfavorable effect on the energy-intensive Bulgarian economy. This effect was somewhat mitigated by the cheaper dollar compared to the lev. The emerging downward trend of oil prices on international markets, along with the continuing dollar depreciation is a source of higher optimism for Bulgarian companies.

The **transport sector** did not witness any development towards substantially improved efficiency of both the sector itself and the benefits its services generate to other sectors. The issue of more active private sector involvement in infrastructure management and in transport activity became topical again. This question was given priority in the aviation and water sectors and related infrastructures, owing to the desire and efforts of government authorities to privatize transport companies and to concession airport and seaport complexes. The entry of private operators in the railway sector becomes all-important, given the effect of BDZ's monopoly position on shippers' competitiveness.

The privatization of BTC EAD and the new Telecommunications Act are crucial for the **high technology and telecommunications sector**, yet in the first quarter of 2003 again, the government managed to solve neither of these two problems. Nevertheless, the delay did not prevent the first steps to ruin the monopoly of BTC EAD. The Internet provider Orbitel filed with the Telecommunications Regulatory Commission documents for telecommunications operator license. The new deputy minister of transport and communications in charge of the Information and Communication Technologies Sector was also appointed in the first quarter of 2003, despite that, given the government-declared special attention to

ICT, this change should have been made a long time ago.

Two events in the first quarter of 2003 had negative effect on global **tourism** development. The war in Iraq and the SARS epidemic. However these negative factors did not have such significant effect on Bulgaria. The winter season was a success owing also to the good meteorological conditions. Implemented infrastructure development measures and the united efforts of tour operators, hotel-keepers and owners of ski lifts in Borovetz and Bansko also contributed to a longer winter season. In the period January - March revenues from tourism amounted to USD 172 m, registering an increase by USD 20 m compared to the same period of 2002. Bulgarians' spending on travels abroad also registered an increase, reaching USD 136 m for the first quarter of 2003. Despite all, balance of tourism is positive, amounting to USD 35.7 m. World's biggest and most prestigious tourist exchange was organized in Berlin in March. It has been noted for Bulgaria that at this stage global developments do not have negative effect on the preparation for the summer season and expectations about sea holidays are optimistic. Government's decision to cut down three times visa prices for nationals of Russia, Ukraine, and Byelorussia (taken in the first half of April) will also have a positive effect on tourists inflow, particularly in the summer seasons.

Agriculture is characterized by continuing improvement of the mechanisms to support agricultural producers, building databases for the condition of the sector as a basic instrument to protect Bulgaria's positions in the negotiation process with the EU, and working out strategies for individual important segments. Project financing under SAPARD continues at accelerated pace. A revival of the land market is observed, characterized by higher number of sale transactions, higher average price and improved tenancy relations. Despite the unfavorable weather conditions and the serious damage by frost of certain areas under winter wheat, higher yields

could be expected in unaffected regions as farmers were subsidized to buy quality seeds, fertilizers and diesel fuel.

The role of the **capital market** in Bulgaria's financial sector remains insignificant - at the end of March the total market capitalization of the Bulgarian Stock Exchange was slightly above 4 per cent of the adjusted GDP forecast for 2003. Non-synonymous development of the main indicators characterizing the condition of Bulgaria's capital market was registered in the first quarter of 2003. The SOFIX index generally preserved its upward trend during the period, and at the same time market capitalization also increased. Compensatory instruments excluded and block deals included, in this quarter the stock exchange trade turnover and volume were lower compared to the previous quarter. Low liquidity remains a major problem of the market. Nevertheless, most securities included in SOFIX (as well as some other) register good liquidity, which has been welcomed by investors and provides good basis for further promotion and development of the market. Early March marked the official start of the so-called COBOS system (client order-book online system) for electronic placement of orders via Internet by clients of stock exchange members. In terms of the normative and regulatory environment, the most important event in the first quarter of 2003 was the constitution of the new joint supervisory body – the Financial Supervision Commission – on the strength of the Financial Supervision Commission Act passed at the end of 2002. In mid-March the National Assembly appointed the members of the Financial Supervision Commission and the latter came into operation.

In Bulgaria financial intermediation is provided mainly through the **banking system**. The condition of banks in Bulgaria remains stable, with excellent capital adequacy and liquidity indicators and parallel effective banking supervision. Foreign participation in the banking system of Bulgaria is predominant in both equity control and assets under management. Generally the banking system marks continuing

increase of assets, and decrease of deposits and current profit in the quarter under review. But at quarter-end current profit was higher compared to March 2002. The net interest income/other non-interest revenues ratio registered increase. Loans to the non-government sector manifest a clear upward trend. In the first quarter of 2002 newly negotiated loans from commercial banks totaled BGN 991.4 m, whereas in the first three months of 2003 they totaled BGN 1 235.34 m (registering a growth of almost 25 per cent). Despite the intensified lending activity and the good indicators for the sector as a whole, the efficiency and level of development of Bulgaria's banking sector remain questionable.

In the **social security area**, the new Social Security Code was not passed on second reading in parliament in the first quarter of 2003. The authorization of the pension company - custodian bank relatedness was undoubtedly the most widely discussed case. The return on investments of pension funds reported for 2002 reveals that saving in a private pension fund proves an excellent and relatively low-risk investment. First financial results of the introduced minimum social security thresholds per sectors and professions and of the mandatory registration of labor contracts at the NSSI generated optimistic expectations for possible future lowering of the social security burden for employers and employed and for possible raise of pensions and higher living standards.

The downward trend in the number of **unemployed** registered at the labor offices was preserved in the first quarter of 2003. In January the unemployment level was 17.46 per cent according to this indicator, dropping down to 15.69 per cent in March. Parallel increase of employment was registered. Latest amendments to the Employment Promotion Act took effect since March, and the National Program "From Social Assistance Towards Employment" entered its most significant phase with 600 approved projects. An important event of the quarter is the agreement, which Bulgaria signed with the World Bank for a loan of EUR 50.8 m for implementation of a Social

Investments and Employment Promotion Project.

The nominal and real increase of the **incomes** of Bulgarians, registered by NSI on the basis of data for wages and household budgets, continued in the first quarter of 2003. A major institutional change also occurred in the area of social assistance. In accordance with the latest amendments to the Social Assistance Act, an Agency for Social Assistance was set up to replace the currently operating special body. Bulgaria has long-standing and well operating social partnership mechanisms on national level, however, at sector, enterprise or municipal level the relationship between employers and employed does not always go well. Conflicts related to the pending privatization of big enterprises, significant to national economy, are most serious. The quarter under review was full of demonstrations of social tension in such situations.

In the **healthcare** sector, the signed 2003 National Framework Agreement generated wide public debate in the first quarter of 2003. It is considered better than previous agreements and able to provide higher transparency in the healthcare system and improved health services for the people, but the fact that general practitioners and pharmacists do not accept the changes reveals that controversial points do exist and there is a need to continue the dialogue. Shortage of funds for medicines is also expected in 2003. It is predetermined by the voting of an unjustifiably low medicines budget, as well as by the inefficient management of funds for medicines. In-patient care reform registers delay, which results in inefficient operation of medical institutions in general and in poor quality of the health services delivered to the people. Frequently amended healthcare legislation and the insufficient awareness about changes of both medical care providers and the health insured generate uncertainty and lack of confidence in the implemented health reform. Expansion of the voluntary health insurance market by another two private funds and the increased interest of insurance companies towards the national health insurance

market indicate good market perspectives, but the low real income of Bulgarians and latest tax changes concerning voluntary health insurance contributions account for the low percentage (below 8 per cent) of the active population insured in voluntary private health insurance funds.

In the **environmental policy** area, the first quarter of 2003 outlined substantially new range of issues concerning the specific application of prescribed environmental norms. Two new regulations deserve attention within the environmental legislation process – the Ordinance on the Terms and Procedure of Conducting Environmental Impact Assessment for Investment Proposals for Construction, Activities, and Technologies, as well as the Ordinance on the Terms and Procedure of Issuing Integrated Permits for the Construction and Use of New and for the Use of Operating Industrial Plants and Facilities. In relation to Bulgaria's positions on the negotiations with the EU, business representatives and MEW announced in the beginning of the year their assessments of the technological, investment and management potential of Bulgarian companies to apply the European environmental policy. "The environmental price", which the Bulgarian industry is expected to pay to fulfill EU directives, became a topic of heated public debates. Despite the sensitivity of the business and the government about this issue, it can be successfully resolved in the wider context of the efficiency of administrative prevention and control procedures and government's willingness to form favorable parameters for environmental activities by way of adequate economic incentives.

The first three months of 2003 did not prove the best time for development of the **negotiations for Bulgaria's accession to the European Union**. The war in Iraq and Bulgaria's position in support of the United States and Great Britain generated many controversial responses and statements by some Member States. There are a number of unresolved issues, which have effect on the negotiations. There is certain delay in the adoption of important draft

laws and regulations. Bulgaria did not close any new chapter of the negotiations. At the end of March the Minister of European Affairs and Chief Negotiator expressed a concern that the negotiations with the European Union may well not be completed by the end of May 2004, which is the preliminary target date. It is time to note that if the regular report of the European commission on the progress of Bulgaria, to be published in October, does not state that the country is ready to complete the negotiations, that will not happen by the end of May 2004. Consequently, hopes remain (but also the need of specific efforts) that Bulgaria will manage to achieve progress and specific understanding on the date for its accession to the European Union.

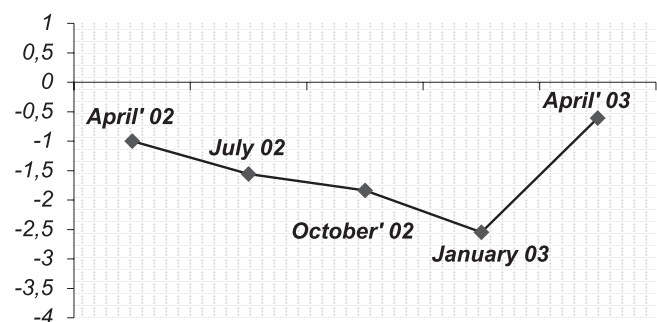
Legislative initiatives targeting improvement of **other elements of the business environment** continued in the first quarter of 2003. The Act on the Administrative Regulation and Administrative Control of Economic Activity was passed on first reading, which aims at restricting the intervention of central and local government in the operations of commercial companies and entrepreneurs. The work on the development of an entirely new Public Procurement Act continues. The special work group set up last year holds its meetings where opportunities to make amendments in the act, targeting higher transparency, flexibility and expediency of procedures, are discussed. An Act Amending the Act on Protection of Competition (APC) was promulgated. It constitutes profound revision of the legal regulation of competitive relations in the country. Amendments to the act are expected to generate amendments of other regulations related to CPC's operation. The accelerated implementation of this process will result in a comprehensive legal framework of competition in Bulgaria. In March the National Assembly passed on first reading amendments to the Commercial Code, which basically aim at accelerating bankruptcy procedures and the procedures for transformation of commercial companies. Amendments envisage drastic cut down of the number of procedures and the terms for their execution, as well as better protection

of the interests of bona fide creditors. Problems in the judiciary system persist, as well as their negative effect on both the business environment and the overall image of Bulgaria in the international community and among foreign investors. Efforts to implement the reform of the judiciary system through the consensus of parliamentary represented forces continued in the first quarter of 2003. Important political consensus on the basic guidelines of reform and an understanding for amendments to the Constitution, which are executable by the 39 National Assembly, were reached at the end of March.

The Estat Index of Business Climate in Bulgaria

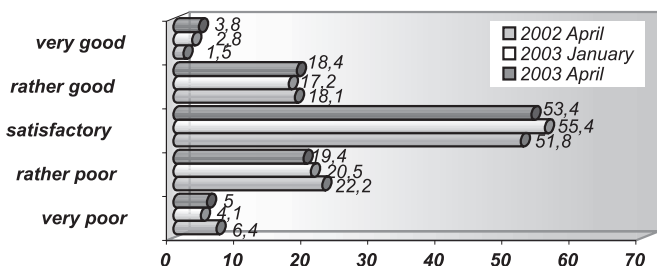
The integrated value of the **Estat index** of business climate¹ in April was **-0.61** and remains in the neutral part of the scale. **The condition of the economic environment can be characterized again as “neither favorable, nor unfavorable”**. The index value is very close to the one registered last year (-0.998). Entrepreneurs’ assessments can be defined as seasonal (Figure 1).

Figure 1. Business climate dynamics



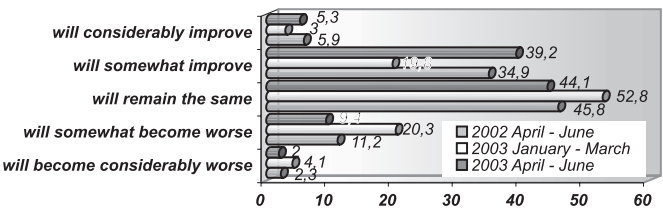
Increased optimism in April influences managers’ assessment of their assets’ condition. The value of Component I of Estat Index - “Company condition” grows from -0.69 in April 2002 to +4.61 in the beginning of the second quarter of 2003. This is due to the slightly increased assessment of company condition and more favorable forecasts for the following quarter. Responses about owned resources are also better (Figures 2 and 3).

Figure 2. Assessment of companies current condition



¹ The survey was conducted in the period 2-11 April 2003 among managers of 398 companies and is representative at the level of going concerns. Criteria for selection of companies in the sample are the region, sector, number of employees and type of ownership. The methodology of the index and the mathematical model are developed by the Estat Agency for Market and Social Studies. The integrated index consists of three components. Component I “General condition of the company”, Component II “Investment attitudes and company strategies” and Component III “Business environment”.

Figure 3. Expectations of companies condition in the following quarter



Skepticism of the business about the future registered in the previous survey seems to gradually decrease with the winter going away. Almost half of the respondents state they expect their companies condition to improve in the months to come. In practice, however, managers assess realistically their capacity. 27 per cent of them do not indicate a single advantage of theirs before competitors (Table 1). The basic reason for this is to be sought both in the shortage of resources and their relatively low quality and the problems related to the business environment.

Table 1. Companies position compared to competitors, %

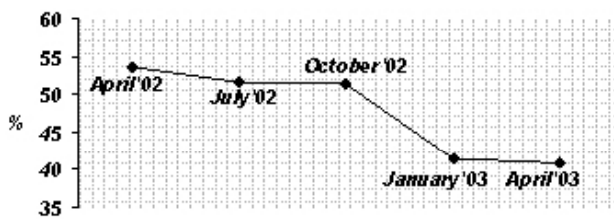
| Number of competitive advantages | 2002 | | | 2003 | |
|----------------------------------|-------|------|---------|---------|-------|
| | April | July | October | January | April |
| None | 19.5 | 28.3 | 32.5 | 33.1 | 27.1 |
| 1 | 19.8 | 13.1 | 16.3 | 17.0 | 16.6 |
| 2 | 18.8 | 24.2 | 17.6 | 18.3 | 22.1 |
| 3 | 16.5 | 14.4 | 13.9 | 12.0 | 11.6 |
| 4 | 13.2 | 7.8 | 10.8 | 10.3 | 9.5 |
| 5 | 7.1 | 6.9 | 3.7 | 4.0 | 6.0 |
| 6 | 5.1 | 5.3 | 5.2 | 5.3 | 7.0 |

Higher expectations about coming months do not significantly impact their tendency to invest. The growth of Component II of the Business Climate Index - “Investment attitudes” is below 4 points and reaches 28. Its value goes up compared to January 2003 (24.2) but still remains rather lower than in April of last year (35.2).

Although over 71 per cent of managers admit they suffer shortage of financial resources, 40 per cent would not borrow a bank loan to invest. Like in previous months this position demonstrates unwillingness to take additional risks. The existence of such a trend

is observed most clearly when tracing the share of respondents agreeing to the statement “If I had free funds I would investment them in another business activity even if there was some risk” (Figure 4).

Figure 4. Share of respondents that agree to the statement “If I had free funds I would invest them in another business activity even if there was some risk”



Those inclined to take a risk to develop a new business decrease by 13 percentage points only within a year. The shortage of financial resources, as well as the relatively low quality of assets and human capital are among the reasons for increased hesitations with regard to investments. However, the basic role is that of the lower assessment of company’s position in the competitive business environment. The lack of confidence in one’s own capacity and advantages decreases the willingness to expand even among those who state that the organization they manage holds a significant position with regard to competitors in the respective sector. By 25 per cent lower within a year is the share of managers of companies that have most competitive advantages, in this case 6, (Table 2) who would invest excessive funds in another business. One fifth lower is the percentage of entrepreneurs whose companies have no advantages to the others in the industry, but would make a risky investment. A similar decrease is observed in all groups. These differences occurring only within 12 months are a serious indication of the changes in the conditions for developing of business in Bulgaria and the actual condition of economic actors.

Table 2. Share of managers inclined to make a risky investment if they had excessive funds according to their assessment of company’s competitive advantages.

| Number of competitive advantages | If I had free funds I would invest them in another business activity even if there was some risk (share of those who agree), % | |
|----------------------------------|--|------------|
| | April 2002 | April 2003 |
| None | 54.5 | 34.0 |
| 1 | 53.2 | 35.9 |
| 2 | 55.4 | 41.4 |
| 3 | 53.8 | 54.3 |
| 4 | 49.0 | 41.7 |
| 5 | 50.0 | 60.9 |
| 6 | 60.0 | 35.7 |

Another emphasis in the interpretation of results of the April survey of business climate in Bulgaria is related to the annual closing of accounts and filing of tax returns. Problems with bureaucracy make managers rather criticizing when speaking about legislation and tax system. Percentages are very close to those of April 2002. Some indicative statements are listed below (Table 3).

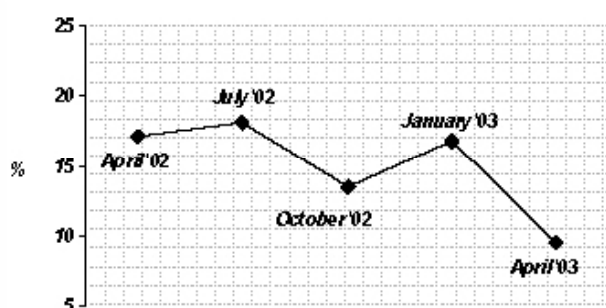
Table 3. Some more important statements related to the problems around annual closing of accounts, %

| | January 2003 | April 2003 |
|--|--------------|------------|
| Work is done best with central and local administration if you know someone who works there | 88.9 | 92.9 |
| Most businessmen would pay some additional sum to avoid difficulties with the administration | 80.7 | 84.5 |
| Practical implementation of the regulatory framework is difficult | 72.7 | 76.9 |

Increased percentages alert on two major problems - difficulties in the implementation of the regulatory framework that become even more tangible at the end of the year and increased tendency to overcome such problems in an unlawful way - by bribes and using connections.

Evaluations of the activities of the government with regard to business drop down dramatically only within a quarter. This holds true mostly in respondents’ assessment of the legislative initiatives of the parliamentary majority. Only one out of ten interviewed considers them consistent and non-contradictory (Figure 5).

Figure 5. Share of respondents that agree to the statement "The legislative initiative of the government is consistent and non-contradictory"



In conclusion, it can be noted that the business environment continues to be unstable. Optimistic expectations about the following months do not impact investment attitudes and managers' actual assessment of their opportunities in a competitive environment. There is a significant decrease of the tendency to take risks and expand the business. Despite the shortage of financial resources most of the interviewed share they would not offset such a shortage with a bank loan. Annual closing of accounts and problems related to the administration increase critical assessments and the inclination to use unlawful means to overcome impediments. Disapproval of government's legislative initiatives considerably increases.

The Business Environment According to ESTAT Agency Surveys

No significant changes are observed in entrepreneurs' evaluation of business environment in the first quarter of 2003. Compared to the first quarter of last year when surveys started, it can be stated more categorically that there is some positive trend in businesses perception about the tax environment. This trend as outlined as early as the second quarter of last year and continues to exist in the current year. This concerns assessments of the role of the patent tax - while in the beginning of 2002 over 57 per cent of the interviewed considered it unaffordable, now only 46 per cent of entrepreneurs think so, i.e. less than half of the respondents consider it an impediment to business. At the start of the survey tax rates forced

companies to evade taxes according to 80 per cent of the interviewed, while now 73 per cent are of such an opinion. Now 15.2 per cent of the interviewed consider that the taxation system creates equal conditions for all companies, while in the first survey such a statement was made by 10 per cent of the businesses. This once again gives grounds to state that changes in the tax policies of the government have a positive effect on the business climate.

Difficulties in **starting up a new business** are still indicated by entrepreneurs as some of the major problems they face. Over 90 per cent of the respondents are still convinced that in Bulgaria this is difficult. At the same time, there is a slight decrease in the percentage of those who think that **administrative barriers** are the major problem for the business. It should be noted once again that this problem is overstated and there is a strong inertia in the answers, since some objective facts indicate that compared to other countries starting up a business in Bulgaria is relatively inexpensive and fast.

Regardless of the specific steps undertaken in this area a radical solution of the problem is still to be accomplished by passing the law on administrative regulation and administrative control over economic activities. This law was passed at first reading in Parliament (in May the second reading of the draft law started) and it is expected to have a positive effect on the business environment. A similar impact is observed with the "one-stop-shop" implemented in a number of Bulgarian municipalities, as well as the prospects of e-Government development in Bulgaria.

There is an increasing positive attitude of the business towards the process of **harmonization of Bulgarian law with aquis communautaire** and expectations of improvement of the business environment towards better transparency and objectivity, and clearer rules. In the beginning of the surveys 55 per cent believed in this statement while now their share reaches 58 per cent. Nevertheless, what is extremely necessary is the more active involvement of entrepreneurs in the process of legislation alignment, broader awareness of the implications and requirements to the business.

Another fact that gives reasons for optimism is related to the enhanced **confidence in the banking system** - in the first quarter of last year 35 per cent were convinced in its stability and reliability. Now those who assess it in such a way are over 40 per cent. This circumstance can be explained with some positive development of lending to businesses.

Overall, however, entrepreneurs think that the government does not apply well targeted and efficient policies to encourage business - the percentage of those who do not see a development and successful protection of such a priority in the government policy ranges between 80 and 90 per cent.

The opinion of the business about the **legislative initiative of the government** continues to be negative - problems ensue from the lack of adequate consistency, contradictions and frequent amendments of laws. A certain positive change is observed in the evaluation of the practical implementation of laws. But overall, business people think that the legislative activity creates uncertainty, vagueness, impossibility of planning company's operations.

The topic of **existing unfair competition** is also one of those traditionally receiving negative assessment - over 82 per cent do believe that unfair competition in Bulgaria is rather common and creates difficulties to business. The amendments to the Act on Protection of Competition promulgated in January that concern cartels, concentration, abuse of joint dominant position, the role of the Commission for Protection of Competition, etc., as well as the wider business information campaign will create a clearer legal framework for fair and open competition in the country.

Assessment of procedures of **public procurement** assignments remains low. Less than 10 per cent of the businessmen considered these to be objective last year, and even now only 11 per cent think these are rather transparent. The positive effect probably results from the legislative amendments made in this area in the spring of last year. It is expected that a completely new public procurement law will be

adopted this year that should make procedures more transparent but what is more important is that new compliance efforts are to be made in this area.

It is also important to note that the opinion of the **judiciary system** confirms the existence of serious problems in this area that have a particularly negative impact on the business and mostly on the possibility for prompt and impartial solution of trade litigations - over 90 per cent of the respondents believe that when it comes to resolving of a business litigation in the court, this can not be done promptly, efficiently and fairly.

Both the attitudes and willingness of the business are still in place to pay an additional amount of money (i.e. a bribe) for the prompt solution of problems with the administration which means that tolerance to **corruption** and its spreading continues to be high.

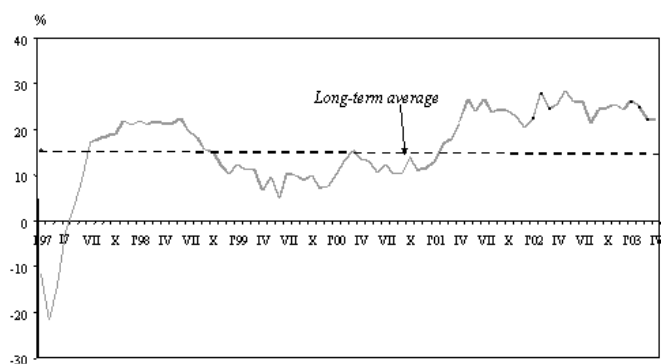
NSI Business Surveys

General indicator of the business climate²

The first quarter of 2003 is characterized with a drop of business climate indicators compared to the previous quarter. In spite of the increase in January of the general indicator of business climate by 2.0 percentage points compared to December as a result of the more favorable economic situation in industry and construction, in February all sectoral indicators of the business climate drop down below January levels and lower the general indicator of business climate by 1.4 points. In March the general indicator of business climate continues its downward trend - 2.8 points lower than February - mainly due to lower optimism of the business climate in the sector of services.

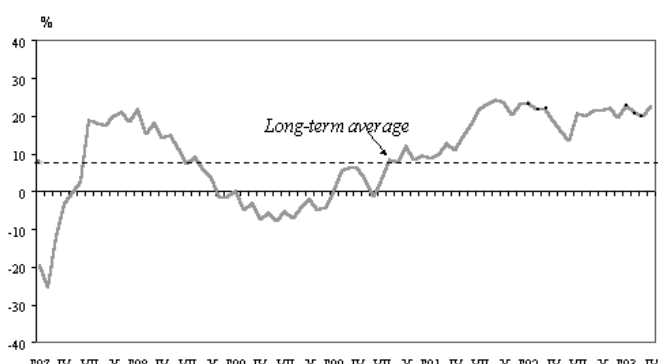
² The general indicator of the business climate that we shall discuss in 2003 presents a weighted average arithmetic value of four sectoral indicators of the business climate - in industry, construction, retail trade and services sectors, and the indicator of business climate in the services sector has been included in the general series since May 2002. NSI started as of January 2003 to report the general index of business climate by including values available as of May 2002 of the business climate indicator in the sector of services. NSI conducts business observations in accordance with the EU harmonized program. Responses to the questions of the survey are presented in a three-category scale of the type: "increase", "no change", "decrease" or "above normal", "normal", "below normal". Balances of assessments are calculated as a difference of relative shares by extreme options of a response. The indicator of business climate is an average geometric value of balances of assessments of the current business situation and the expected business situation in enterprises for the next six months.

Figure 6. Business climate, general (NSI)



Source: NSI

Figure 7. Business climate in industry (NSI)



Source: NSI

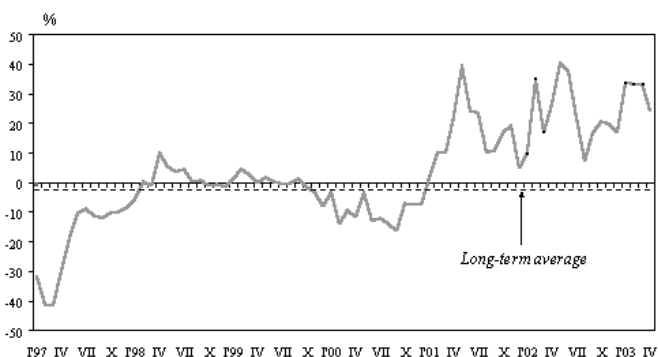
Industry

In the first quarter of 2003 business climate indicators in the industry have generally lower levels compared to the first quarter of last year, located in a similar downwards curve. Though compared to December of last year the January value of the compound sector indicator of the business climate goes up by 3.3 points as a result of the positive expectations to the business condition of industrial enterprises over the next 6 months and considerably higher optimism in the expectations of production activity over the next 3 months, the January production output is not assessed as increased compared to December. In February the deteriorated values of the current business condition of industrial enterprises have a negative impact on the compound business climate indicator, which goes down by 1.8 points compared to January. February is the third month in a row in which assessments of the current production activity go downwards. It is hardly in March that business managers are of the opinion that there is an increase in industrial production output accompanied by a higher level of orders from abroad. Domestic orders, however, continue to decrease. The March level of the compound indicator of the business climate in industry loses 1 point of its February value. Thus, at the end of the first quarter the business climate indicator in industry has insignificantly improved (by 0.5 points) compared to the end of the previous quarter, but it is by about 2 points lower compared to March 2002.

Construction

It is worth noting that throughout the three months of the first quarter the indicator of business climate in construction holds relatively high levels. In January the high expectations of the business condition of construction companies for the next 6 months determine substantial increase of the compound indicator of business climate in construction by 16.9 points compared to December. While in February more reserved assessments of the current business condition of construction companies slightly lower the business climate indicator in the sector (by 0.8 points), optimistic expectations for the following 6 months maintain it at a relatively high level in March again.

Figure 8. Business climate in construction (NSI)



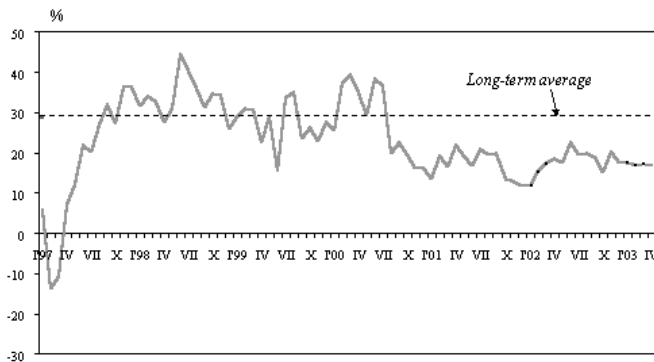
Source: NSI

Retail Trade

In the first quarter of 2003 the business climate indicators in retail trade have higher levels compared to the first quarter of last year and fluctuate around the

level at the end of the year. In January the compound indicator of business climate in retail trade keeps its level from December. Assessments of the current business condition in retail enterprises are less favorable in February. This determines the slight drop down of the compound indicator of business climate in retail trade by 0.9 percentage points. In March the indicator goes a little bit up and expectations continue to improve with regard to sales and orders to suppliers for the next 3 months.

Figure 9. Business climate in retail trade (NSI)

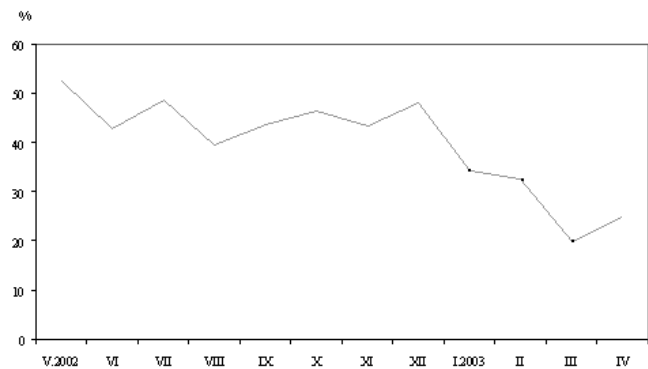


Source: NSI

Services (excluding trade)

In the first quarter of 2003 most unfavorable seems to be the dynamics of business climate in the sector of services. In January compared to December the compound indicator of business climate in the sector of services sharply drops down by 13.7 points due to the shift of opinions from optimistic to moderate assessment of the business condition of the enterprises in the services sector. This shift explains the further decline of the indicator by 1.9 points in February, and in March it results in another sharp decline - by 12.5 percentage points. In March there is a lower optimism in the opinions about assessment of the current and expected demand for services.

Figure 10. Business climate in services, excluding trade (NSI)

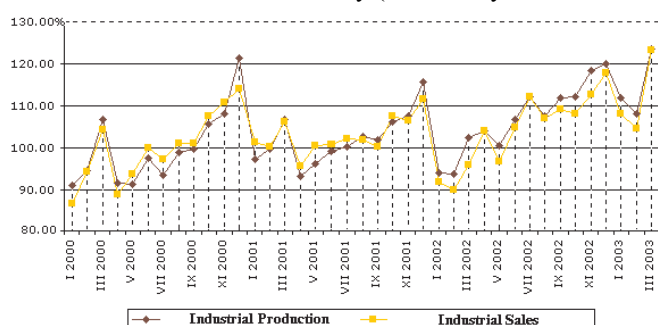


Source: NSI

Gross Domestic Product

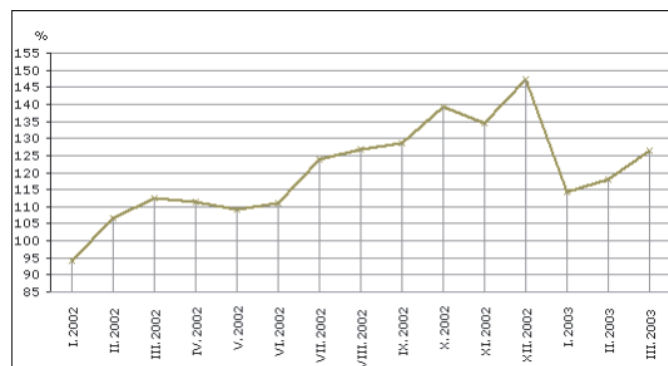
As far as a significant growth is observed in industry and trade in the first quarter of 2003 compared to the respective months of 2002 it could be expected that on an annual basis GDP growth in the first quarter of 2003 will not be lower than the growth in the first quarter of 2002 (3.4 per cent according to data revised as of April 2003). Despite the NSI registered relatively lower levels of business climate in industry and services³ that probably reflect the negative expectations in the eve and during the Iraq conflict, in the first three months the growth of sales in industry and trade and of industrial production (Figures 11 and 12) exceeds substantially the growth in the first quarter of last year. In support of our expectations of a high growth in the first quarter of 2003 are also the statistics of exports and imports of goods that significantly exceed those of the first quarter of last year and evidence activation of both supply and demand.

Figure 11. Indexes of industrial production and indexes of sales in industry (reference year 2000 = 100)



Source: NSI

Figure 12. Indexes of net sales in the sector of trade, repair of motor vehicles and personal and household goods (reference year 1995 = 100)⁴



Source: NSI

What is disturbing in the shaping of our expectations of the macro-economic dynamics in the first quarter of 2003 is the sharp decline of the growth rate in the sector of services from 6.6 per cent in the third quarter to 3.1 per cent in the fourth one of 2002 (this is the lowest growth rate of services in the fourth quarter for the last five years). On the other hand, striking is the fact that the business climate in the sector of services (without trade) had rather high levels in the third quarter and even a slight increase in the fourth quarter of 2002, and in the first quarter of the current year it suddenly drops down.

The preliminary data of the National Statistical Institute on the gross domestic product in the fourth quarter and for the whole 2002 confirmed our expectations that the annual rate may exceed the official estimates⁵. Revised statistics of GDP rate by quarters (for the first quarter from 3.2 to 3.4 per cent, for the second - from 5.3 to 5.6 per cent, and for the third - from 4.5 to 6.4 per cent) and preliminary data of the fourth quarter (3.4 per cent growth rate) indicate that the achieved higher annual growth for 2002 (4.8 per cent) is mainly due to the significantly stronger third quarter. Data for 2001 are also revised and according to these GDP annual rate is 4.1 per cent and the quarterly rates are respectively: for the first quarter 3.9 per cent, for the second - 3.6 per cent, for the third - 4.3 per cent, and for the fourth - 4.3 per cent (Table 4).

³ Services excluding trade

⁴ Indexes are calculated on the basis of average prices of 1995.

⁵ According to the Preliminary report on the execution of the consolidated fiscal program of the Ministry of Finance of 22 January 2003, a growth of 4.2 per cent was expected for 2002. According to the Monthly macroeconomic review of the Ministry of Economy, the expected annual growth for 2002 was 4.4 per cent as of 9 April, 2003.

Table 4. Index of the physical volume of GDP by components
(the corresponding period of the previous year = 100)

| | 2001 | | 2002 | |
|-------------------------------|--------------|--------------|--------------|--------------|
| | IV quarter | year | IV quarter | year |
| Gross value added | 104 | 103.9 | 103.2 | 104.7 |
| By economic sectors: | | | | |
| Agriculture | 100.5 | 100.3 | 104.0 | 105.1 |
| Industry | 104.9 | 104.1 | 103.1 | 103.5 |
| Services | 104.3 | 104.7 | 103.1 | 105.1 |
| By type of ownership: | | | | |
| Private | 106.9 | 106.6 | 105.7 | 107.6 |
| Public | 97.9 | 97.7 | 97.0 | 97.3 |
| Adjustments | 106.8 | 105.5 | 105.3 | 105.6 |
| Gross Domestic Product | 104.3 | 104.1 | 103.4 | 104.8 |
| Final consumption | 106.1 | 104.4 | 107.3 | 104.1 |
| Individual | 106.7 | 104.6 | 107.1 | 103.9 |
| Collective | 102.1 | 102.9 | 108.5 | 106.2 |
| Gross fixed capital formation | 133.1 | 123.3 | 114.7 | 109.3 |
| Exports of goods and services | 99.7 | 110 | 109.3 | 106.2 |
| Imports of goods and services | 108.6 | 114.8 | 110.3 | 104.7 |

Source: NSI

Following the already actual end of the military actions in Iraq, macro-economic parameters of the implications for Bulgaria in our opinion correspond to the estimates according to the official scenarios of a short-term conflict. According to the evaluation report of the crisis impact on the Bulgarian economy and 2003 budget presented to the public by the minister of finance in the mid of March, in the short-term conflict scenario the GDP annual growth rate for 2003 is expected to be 5 per cent, as a result of the expected though low increase of exports (due to lower competitiveness as a result of strong local currency) and of increased domestic demand (due to low prices of imported goods). The up-dated projection of the Ministry of Finance for 2003⁶ for GDP in Bulgarian Levs is BGN 35 285.5 m; the Bulgarian National Bank⁷ works with a projected GDP of USD 18 900 m.

⁶ Source: MoF, State Debt monthly bulletin, March 2003 (according to data as of 15th April, 2003)

⁷ Source: BNB, Balance of Payments January-March, 2003 press release (according to data as of 30 May, 2003)

⁸ The industrial producer price index on the domestic market is assumed to be the basic producer price index which has the following major applications: a basic short-term business indicator that predicts trends in inflation rate changes; the index can be viewed upon an early measure of the current inflationary process in economy; deflator for calculation of volumes in constant prices -for example, as a deflator for the National Accounts, or deflation of sales on the domestic market when calculating the index of industrial production; various ministries and industrial organizations use the index to monitor the price pressure in some sub-sectors of industry; trade associations and companies use the index as an impartial measure of prices when concluding contracts and for analysis of changes in purchases and sales; a short-term indicator required by a number of international organizations: Eurostat, IMF, the European Central Bank, that use it for international comparisons and economic monitoring. More information can be found on NSI web-site: <http://www.nsi.bg/News/Op/OpList.htm>

Inflation

There is nothing that deserves more attention in the general dynamics of consumer prices in the first quarter of 2003 than to compare the dynamics of consumer prices to the dynamics of industrial producer's price indexes on domestic market. Since the beginning of 2003 the National Statistical Institute has started to publish in Internet producer's price indexes that will allow their actual use for a quick short-term analysis in their capacity of some of the basic short-term economic indicators characterizing the economic situation in the country⁸. What is striking is that the change of consumer prices is much less significant than the change of producer's prices (Tables 5 and 6) which is explained on the one hand with the imports competition on the market of consumer industrial goods, and on the other hand - the share of domestic industrial goods in the consumer basket does not seem to be structurally defining.

Table 5. Monthly dynamics of consumer prices, %

| | I | II | III |
|---|-----|-----|------|
| Inflation (CPI-100), previous month =100, % | | | |
| 2003 | 0.6 | 0.1 | 0.4 |
| 2002 | 2.7 | 1.6 | 0.8 |
| Inflation (CPI-100), December of previous year =100, % | | | |
| 2003 | 0.6 | 0.8 | 1.2 |
| 2002 | 2.7 | 4.4 | 5.2 |
| Inflation (CPI-100), the corresponding month of previous year =100, % | | | |
| 2003 | 1.7 | 0.2 | -0.2 |
| 2002 | 7.0 | 8.4 | 9.2 |

Source: NSI

Table 6. Monthly dynamics of producer's prices in industry for the domestic market, %

| | I | II | III |
|--|-------|-------|-------|
| Previous month =100 | | | |
| 2003 | 101.8 | 101.3 | 101.0 |
| 2002 | 100.4 | 101.1 | 101.0 |
| December of the previous year =100 | | | |
| 2003 | 101.8 | 103.1 | 104.1 |
| 2002 | 100.4 | 101.5 | 102.5 |
| Corresponding month of the previous year=100 | | | |
| 2003 | 107.8 | 108.0 | 108.1 |
| 2002 | 100.1 | 99.6 | 100.3 |

Source NSI

According to the scenario of a short-term conflict in Iraq (which it proved to be) in the report of the Ministry of Finance on the evaluation of the impact on the Bulgarian economy and 2003 budget, the average annual inflation rate in the country is expected to drop down to 2.6 per cent in 2003.

Labor Market

The analysis of the labor market data for the first quarter of 2003 outlines two factors whose impact is difficult to separate from the dynamics of the labor market itself, but should at least be borne in mind. The first one is related to the employees going out "into the light" as a result of obligatory registration of labor contracts as of the beginning of 2003. This factor should have an upwards effect on NSI data of the "Quarterly survey of employees, worked time, wages and salaries and other labor costs" but also a downward effect on the data of the Employment Agency about the number of registered unemployed - by deleting of employees who before that have been registered at the same time as unemployed. The second factor is related to the fact that in 2003 a change was made in the methodology of the labor force survey, as a result of which (as NSI made an explicit warning) data from the monitoring of the labor force survey in the first quarter of 2003 are not comparable to the data from previous periods.

According to NSI data at the end of the quarter 2 013 thousand people are hired under a labor contract (i.e. by 123 thousand or by 6.5 per cent more compared to the end of the first quarter of 2002, and by 102 thousands or by 5.3 per cent more compared to the end of the year 2002).

At the end of March the number of unemployed registered at the Employment Agency is 581 350 (by 87 622 less or by 13 per cent less than the end of March 2002 and by 21 174 or 3.5 per cent less compared to the end of 2002) and the coefficient of registered unemployment is 15.7 per cent (calculated at 3 704 336 economically active population as per the 2001 census).

If we calculate the average number of unemployed registered at the end of each month of the first quarter, the average for the quarter is about 613.3 thousand. In the first quarter of 2003 the average number of people that defined themselves as unemployed according to the new methodology of NSI⁹ is 499.6 thousand, and the unemployment coefficient is 15.6 per cent with an average figure for the quarter of 3 203.9 thousand economically active population. Though a very rough comparison (due to the methodological incomparability of data) it is striking that at the end of 2002 the absolute difference between registered and self-defining as unemployed is about 60 000, and in the first quarter of 2003 the difference between the average number of registered unemployed and the average number of self-defined as unemployed is almost 114 thousand.

In the first quarter of 2003 the number of registered unemployed sharply declines, and the difference between registered and self-defined unemployed sharply increases. These data tend to implicate that if most of those registered as unemployed who have been hired at the same time are taken out of the number of registered unemployed, probably a lot of people tend to register as unemployed and at the same time practice some form of self-employment hidden from NSSI and EA, which has no bearing on NSI monitoring (because hiding or not hiding from NSI is not related to any interests, unlike EA or NSSI). The latter raises again the question about comparability and correctness of the techniques of measuring employment and unemployment. The increase of "alleged unemployment" burdens the society in its efforts to handle actual unemployment and remains a serious challenge to the government's responsibility to create conditions for balanced interests of all actors in the economy.

⁹ On 26 May NSI announced that as of the beginning of 2003 changes are made in the methodology and the toolkit for monitoring of the labor force and therefore the data from labor force monitoring for the first quarter of 2003 cannot be compared to data for previous periods. Changes are made in compliance with Eurostat requirements in this area and mainly consist of the following:

- a change in the frequency of the study - the survey (field work) is done permanently and results are processed quarterly, therefore obtained values present average values for the period (quarter);
- a change in the definition of unemployed, according to Regulation No 1897/2000 of the European Commission - it consist mainly of complementing and specifying active methods of job seeking, that define persons as unemployed, namely: an active method of job seeking is considered to be contacting the labor office, and not the very fact of registration; unlike the previous definition, studying ads in newspapers, magazines, etc., is also defined as an active method of seeking a job;
- the volume of the sample is reduced from 24 000 to 18 000 households.

Execution of the Budget during the First Quarter of 2003

The first quarter of 2003 can be characterized with a relatively good execution of the budget and individual items show positive changes compared to the same period of last year.

Consolidated budget (covers the national budget and the budget of the judiciary)

Revenues under the consolidated budget for the first three months of 2003 amount to BGN 3 220.6 m, or a little over 24 per cent of the annual amount of revenues under the consolidated budget program versus BGN 2 717.9 m revenues for the same period of 2002 (21.8 per cent of the last year program). Expenditures amount to BGN 3 109.8 or 22.8 per cent of the annual amount of expenditures under the program (for the first quarter of 2002 the figures are BGN 2 820.8 m or 22.2 per cent of the annual program). As of 31 March there is an excess of BGN 110.7 m under the consolidated fiscal program, due to a large extent to the execution of tax revenues - BGN 2 561.2 m or 24.02 per cent of the planned figure.

National budget (comprising central government budget and budgets of government authorities)

As of 31 March the **national budget has an excess** of BGN 90.8 m with revenues amounting to BGN 1 936.9 m (25.3 per cent of the planned annual figure) and expenses of BGN 1 360.4 m (23 per cent of the annual plan), with provided transfers at the amount of BGN 485.7 m. As a comparison, last year these figures were respectively: revenues - BGN 1 588.6 m (12.8 per cent of the program), expenditures - BGN 1 713.9 m (13.47 per cent of the planned figure).

For the first quarter of the year the **deficit in the central government budget** amounts to BGN 90.8 m, revenues amount to BGN 1 536.8 m, and expenses - BGN 447.3 m. Accumulation of deficit results from transfers provided from the central budget at the amount of BGN 1 180.3 m.

The **fiscal reserve** at the end of March amounts to BGN 3 442.1 m.

As of 31 March 2003 **local governments** have an excess of BGN 53.9 m with BGN 345.2 m revenues, BGN 111.3 net transfers and BGN 402.5 m expenditures.

Taxes and duties

For the first quarter of this year the Customs Agency collected BGN 711.8 m. The total amount collected from customs duties and charges, VAT and excise duty by the customs administration is by BGN 104.7 m more compared to the first quarter of last year.

In January the Budget and Finance Commission with the National Assembly submitted for discussion a draft law on amendment of the Customs Act. The law was adopted in the beginning of April. The major goal of the changes is to continue the process of harmonization of Bulgarian customs law with EU law in this area. Parallel to this, the updated law reflects the accumulated practice of the customs administration over the last years.

At the end of January a **draft law** was introduced to the Parliament on the **amendment of the VAT Act** but it was not passed by the end of the first quarter. Proposed amendments are related to the invitation to Bulgaria to join NATO and arising thereof opportunities for the country to be the host of international military training exercises.

At the same time the Budget and Finance Commission submitted also a **draft law on the amendment of the Tax Procedures Code** that was passed in the beginning of the second quarter of 2003. The objective of the changes is to improve enforcement efficiency and to enhance measures of the administration in the fight against the gray economy. Proposed amendments provoked serious debates about their legitimacy and need concerning the arising possibility to violate private property rights. Experts are of diverse opinion with regard to the provisions envisaging a special regime of application

of Double Taxation Avoidance Agreements (DTAA) which Bulgaria has signed with other countries. These provide for introduction of excessive control by the customs administration that would result in burdening and bureaucratizing DTAA procedures.

At the beginning of 2003 the minister of finance introduced a new practice of communication with the Bulgarian public through Internet. In February and March the minister spared an hour to respond directly to questions asked through the web about the war in Iraq and its impact on Bulgarian economy and 2003 budget, privatization, fiscal decentralization of municipalities, tax policy, effects from the transactions for optimization of the foreign debt of Bulgaria, etc. The idea is to make this a tradition that would contribute to the transparency of the policies of the Ministry of Finance.

At the mid of February the minister approved the lists of municipalities which for the last two years (art. 60 of the CITA) or for the last year (art. 61 d of CITA) before 2003 have had 50 per cent higher unemployment rate than the average one for the country. According to the prescriptions of CITA businesses operating within the administrative boundaries of listed municipalities may receive tax relieves provided they meet certain requirements described in the law.

In the first quarter of 2003 two investment projects were approved where a special scheme of VAT calculation is applied for imports (under the provisions of art. 58 a, b, c of the VAT Act). The amendments effective as of the start of the year entitle importers to charge themselves the tax due on imports and within the same tax period record the amount of charged tax as a tax credit. Thus, investor's funds will not be frozen and this is a positive development for the improvement of the investment climate in the country. The first project belonged to Sofia Med AD, a part of the Greek group Viohalco, and provides for import of machines and equipment at the amount of over EUR 35 m and opening of more than 200 new jobs. The second approved project is that of Drujba AD, city of Plovdiv. The investment in the flat glass manufacturing plant is designed for construction of

a new furnace and six automated flow lines at the amount of EUR 20 880 000. It is expected to open 144 new jobs.

Foreign and domestic debt

At the end of the first quarter of 2003 the total amount of the state and state-guaranteed debt amounts to BGN 17 560 m (calculated at the BNB rates of BGN as of 31 March 2003), or 49.8 per cent of the gross domestic product (according to up-dated estimates of the latter, source: Ministry of Finance). Compared to the end of 2002 the total debt has decreased by BGN 620 m, partially due to the significantly cheaper US dollar versus the Euro, measured at the end of the two periods. With comparable data (up-dated estimates of 2003 GDP and preliminary reported data for 2002) the ratio debt/GDP declines from 55.6 per cent at the end of December to 49.8 per cent at the end of March 2003.

In US dollar terms, however, the total state and state-guaranteed debt has grown by USD 137 m over the period from the end of 2002 till the end of March 2003 (from USD 9 645 m to USD 9 782 m according to the BNB rates on the respective dates). This is due to the more expensive Euro against the US dollar in addition to the change of the debt currency structure. This change is explained not so much with the repayments made during the quarter on the foreign debt (e.g. the principal of the Brady bonds), but rather with the positive net domestic financing. As of the end of 2002 the US dollar denominated debt accounted for 49.79 per cent of the total amount of state and state-guaranteed debt, while at the end of March 2003 the US dollar debt is 47.93 per cent. As a comparison, the share of the Euro denominated debt increases from 28.35 per cent of the total debt at the end of December to 29.9 per cent at the end of March 2003 (the BGN debt also records a growth in the debt structure - from 8.21 per cent at the end of 2002 to 8.66 per cent at the end of March 2003).

In 2003 the amount of the debt will be again predetermined by the dynamics of EUR/USD

exchange rate and currency structure changes. In all cases, however, most important remains the ratio of the total debt to GDP, which will certainly be held within Maastricht criteria.

Foreign debt

In 2002 our foreign debt was restructured twice (in March and in September) whereby through a series of transactions Brady bonds were replaced by USD and EUR denominated Eurobonds. The actual accounting for the September restructuring in the debt dynamics was done in the fourth quarter of 2002. In the first quarter of 2003 no similar transactions in the foreign debt were conducted.

As a result of repayments made and tranches received, as well as of exchange rates fluctuations, **the total foreign debt has increased by USD 45.7 m for the period from the end of December 2002 till the end of March 2003. In BGN terms, however, the more expensive Euro results in decrease of the foreign debt for the period by BGN 677.5 m. The total amount of the foreign debt as of the end of March 2003 amounts to USD 8 506 m or BGN 15 270 m**, recalculated at the BNB rate of BGN/USD as of 31 March, 2003. Data for the last months are preliminary ones.

Domestic debt

As of the end of March, according to data from the Ministry of Finance, the total domestic debt amounts to BGN 2 290.6 m (out of which BGN 2 289.4 m state debt and BGN 1.2 m domestic government guarantees). Compared to the end of the third quarter of 2002 the total domestic debt has increased by BGN 178.8 m.

As of the end of March 2003 in the structure of the domestic debt, the share of the debt for government securities issued to finance the budget deficit accounts for 74.04 per cent of the total amount of domestic debt (versus 69.24 per cent at the end of 2002). As of the end of March, the share of the debt for government securities issued for the structural reform

accounts for 25.91 per cent of the total domestic debt (versus 30.67 per cent at the end of 2002). Again as a percentage of the total domestic debt domestic government guarantees account for 0.05 per cent as of the end of March (versus 0.09 per cent at the end of 2002). Table 7 illustrates the dynamics of the total domestic debt structure.

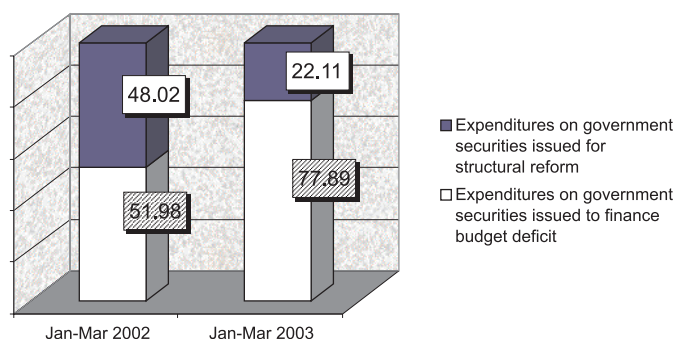
Table 7. Structure of the total domestic debt (%)

| Debt structure | End of March 2002 | End of 2002 | End of March 2003 |
|---|-------------------|-------------|-------------------|
| Debt on Government securities issued for financing of the deficit | 61.13 | 69.24 | 74.04 |
| Debt on Government securities issued for the structural reform | 38.58 | 30.67 | 25.91 |
| Domestic government guarantees | 0.29 | 0.09 | 0.05 |

Source: According to MoF data, State Debt monthly bulletins

Total expenditures on the domestic debt (interest and discount) for the first quarter of 2003 amount to BGN 38.1 m (versus BGN 35.7 m for the same period of 2002). Among those the portion of the expenditures on government securities for financing of the budget deficit accounts for 77.89 per cent (versus 51.98 per cent for the same period of 2002), and the portion of the expenditures on government securities issued for the structural reform accounts for 22.1 per cent (versus 48.02 per cent for the same period of 2002). Figure 13 illustrates the dynamics of the expenditures structure of the domestic debt in 2002 and 2003, respectively.

Figure 13. Expenditures structure of the domestic debt (%)



Source: According to MoF data, State Debt monthly bulletins

In the period January - March 2003 the average yield on the primary market of newly issued government securities for financing of the budget deficit reached 2.53 per cent on an annual basis with three-month

bonds (three auctions for the period), 4.27 per cent on an annual basis with twelve-month treasury bills (one auction for the period), 4.93 per cent with three-year treasury bonds (one auction for the period), 5.52 per cent with five-year bonds (two auctions for the period), 5.80 per cent with seven-year bonds (one auction for the period) and 6.93 with ten-year bonds (one auction for the period) according to BNB data (Government Securities Market, bulletin of Fiscal Services Division).

Thus, with regard to the domestic debt market, **the first quarter marks again a decline in the yield of all newly issued government securities compared to the last quarter of 2002. Like in the previous quarters, the share of securities issued for financing of the budget deficit continues to grow at the expense of the share of securities issued for the structural reform.** Accordingly, the portion of expenditures on government securities, issued for deficit financing, grows versus 2002 as a direct result from the change of domestic debt structure.

One of the important events on the domestic debt market during the quarter was the **issue for the first time of Euro denominated government securities** for financing of the budget deficit. The issue has a maturity of 7 years and 3 months and is of open-end type. This is an extra issue that was not planned in the 2003 calendar of issues. The auction of the debut issue was conducted in February at a gained yield of 5.58 per cent. The total amount of the issue was defined then between EUR 100 m and 150 m, and the first auction sold securities of a nominal value of EUR 50 m. In March a new auction was held for the same issue – the achieved yield was a bit higher, 5.65 per cent, and sold securities had a nominal value of EUR 55.

Overall, the yield of this Euro denominated issue was low, compared for instance to similar BGN issues during the recent months. This reflected the high demand and the need for similar investment alternatives for the investors. On the other hand, however, there was practically no secondary trading in this issue at the end of March, which most probably

could be explained with the high liquidity of the banking system. The lack of secondary trading is one of the possible reasons for the Ministry of Finance to announce in March that this issue would not be offered any more till the end of 2003. The formal justification of this decision was the absence of any need for additional financing.

Debt management strategy

Active management of foreign debt started as early as the fall of 2001, and there were some indications in 2002 of active management of the domestic debt, too. Some of the major criticism to the government was that there was no strategy for management of the debt. Compliance with the Maastricht criteria and increase of the domestic debt at the expense of the foreign debt were the two repeatedly announced objectives but there was no information to what extent meeting these objectives was a part of some long-term strategy.

Deemed as a necessary step towards such a strategy was the Act on the State Debt adopted in September, 2002. At the end of the first quarter of 2003 the Ministry of Finance already presented a State Debt Management Strategy, too.

The strategy is based on the Act on the State Debt, it covers a three-year period and consists of three basic sections. The first section presents the institutional structure, regulatory framework, management organization and debt status as of the end of 2002. The second section examines the risks related to the amount and structure of the debt and defines the goals and objectives of the management policy. The third section contains the specific measures the government plans to undertake to accomplish identified objectives.

The strategy is supposed to be up-dated every year by the Council of Ministers together with the three-year budget projections.

The success of the structural reform in the real sector depends to a large extent on the speed and quality of the privatization process. Successful restructuring and privatization of state-owned companies in the sectors of energy, telecommunications and railway transport would allow the government to focus its efforts on improvement of the business environment and quality of public services, as well as to maintain stable market rules and regulation ensuring competitive environment for businesses.

State Ownership

The careful analysis of state ownership existing at the end of 2002 gives grounds to divide companies with state ownership into the following groups:

Companies with state interest less than 50 per cent

This is the largest group. Options for the sale of these companies are through public tenders organized by PA for limited companies and non-public companies, and offering blocks of shares of public companies on the floor of BSE - Sofia AD.

The problem faced in the liquidation of the state ownership in these companies is the relatively low interest to them, as well as the absence of complete information on the current condition of the state interest in all of these companies. Following the amendments to the APPC of 2002 and PA becoming the only authority conducting privatization, gathering and up-dating of information from all ministries and agencies proved to be a complex and lengthy process. There still does not exist a complete register with up-dated information to allow PA to put a legitimate end to state ownership in about 1000 companies.

Companies with state interest over 50 per cent which by value of their assets could be considered small and medium-sized enterprises

The number of companies in this group is about 300. A part of them are decapitalized and difficult to sell. It has been for several years that PA has wasted human and financial resources in futile efforts to

privatize them. This process should have a logical end - for instance, these companies can be declared in liquidation and the state to promptly dispose of its ownership.

The remaining companies which are in good condition underlie the annual plan of PA and should find new owners by the end of 2003

Companies with state interest over 50 per cent which are structurally defining or have a monopoly position in the country

Privatization of these companies depends on the efforts of PA, the government and the Parliament. Their operation affects large groups of the population and is frequently accompanied by considerable social implications. These companies are mainly in the area of infrastructure industries - energy, communications, transport.

In accordance with established practices or statutory provisions the sale of such companies is subject to development of privatization strategies to be approved by the National Assembly. The process of pre-privatization preparation of these companies require longer period of time and more financial resources. Usually, external consultants are employed for the development of their restructuring and privatization strategies.

Annual privatization plan - 2003

The 2003 Annual Work Plan of PA, approved by the Supervisory Board¹⁰ takes into account the existing structure of state ownership. Minimum objectives are set both with regard to the number of privatization transactions and expected revenues.

According to PA, this year the following sales are expected:

- shares and blocks of shares of **145 companies** in which the state holds over 50 per cent interest;
- **60 detached parts** of companies;

¹⁰ 2002 Work Plan of PA: www.priv.government.bg

- **900 shares and blocks of shares** of companies in which the state holds less than 50 per cent interest.
Expected proceeds from the privatization of state-owned enterprises in 2003 amount to BGN 550 m.

Implementation of the Annual privatization plan in the first quarter

Despite all the commitments and promises of the government and the ruling majority, the pace of privatization in the state-owned sector remained extremely unsatisfactory in the first quarter of 2003. Only 12 transactions were concluded for the sale of companies with majority state interest (over 50 per cent) and 7 transactions for detached parts. Non-implementation is even higher in the area of sales of minority blocks of shares. 25 transactions were realized. Thus, for the three months it proves out that approximately one-month portion of the Annual privatization plan is implemented (Table 8).

Table 8. Implementation of the Annual privatization plan

| | Annual plan | 1 st quarter |
|--|-------------|-------------------------|
| Shares and blocks of shares in companies with over 50% state interest | 145 | 12 |
| Detached parts | 60 | 7 |
| Shares and blocks of shares in companies with less than 50% state interest | 900 | 25 |

Privatization of structurally defining enterprises

Following the failure of the 2002 Annual privatization plan government's efforts were focused on the successful completion of privatization procedures of **Bulgartabac Holding AD and BTC EAD**.

From the opening of the procedure to its unsuccessful end the privatization of Bulgartabac Holding AD was politically burdened. A part of the ruling coalition demanded and managed to impose too many conditions for the sale of the holding company. The major requirement was ensuring the buy-out of tobacco in the years following the privatization which additionally burdens the clumsy and loss-generating structure of the holding.

According to experts' opinion, the strategy for the privatization of the company lies on social, rather than market principles. The company structure comprises enterprises of diverse activities and companies of unequal potential. Finding a "strategic investor" to assume the social functions of the state and restructure the company proved to be a hard to accomplish objective. Despite the evidently unacceptable formula for the sale of the company the government was firmly decided to bring to a successful end the negotiations with the selected buyer - Tobacco Capital Partners.

To this end, and in order to overcome the contradictions between the government and the judiciary, the ruling majority proposed amendments to the Act on Privatization and Post-privatization Control. The goal of the amendments was to exclude judicial control over 15 large privatization transactions, in the core being the sale of Bulgartabac Holding AD.

Initially, the President of the Republic of Bulgaria returned the draft on the amendments to APPC for revision, and later the Constitutional Court rejected the proposed changes as conflicting to the Constitution of the Republic of Bulgaria.

The sale of Bulgartabac Holding AD continued under the provisions of the effective law. Negotiations with the selected buyer (Tobacco Capital Partners) did not lead to an agreement and the transaction was not finalized.

As of the end of March the sale of BTC EAD was not completed, either.

Adding to such a slow pace of privatization the absence of developed and adopted by the end of the quarter strategies for the privatization of Bulgarian River Shipping, Maritime Navigation Bulgare, the 7 electricity distribution companies, as well as non-completed preparation for privatization of companies from the military industry (VMZ - Sopot, Terraton and Kintex) we can draw the conclusion of a shortage of administrative capacity, good coordination and political will to finalize within a reasonable time

horizon the structural reform and the privatization.

Stock Exchange Privatization

On 23 January 2003 the Supervisory Board of the Privatization Agency approved a draft of a list of companies with state interests for the privatization of which payment in non-cash instruments will be allowed in 2003. The list includes 1157 companies. The state is the sole owner of 28 out of these and they are offered for sale completely against non-cash payment instruments. Blocks of shares are offered for sale from another 20 companies where the state is the majority interest owner. The number of already privatized companies from which minority blocks of shares were offered was 1109.¹¹ The list of finally approved companies (adopted by Decision No. 117 of 21 February 2003 of the Council of Ministers) was reduced to 1084 companies. The decision of the CoM is effective with a retrospective date - 1 January 2003.

Some of the amendments to the APPC not rejected by the Constitutional Court envisaged that companies for which it was decided to sell shares by public offering were to be entered in the register of the Financial Supervision Commission as public companies *ex officio*.

Immediately upon the decision of the court, a little after the end of the first quarter, PA announced public offering on the stock exchange of minority blocks of shares in 11 companies of strategic importance for Bulgaria, united in two pools - *Mechta* and *Energetika*. The assessment of all stakeholders - investors, investment intermediaries and holders of non-cash payment instruments - was extremely positive. It was considered that this would support and enliven the capital market of the country.

International Commitments

It is worth noting that in the beginning of March the Bulgarian government undertook a commitment to the World Bank to privatize by the end of 2003 *Bulgartabac Holding AD*, *DSK Bank*, *Bulgarian*

River Shipping, *Maritime Navigation Bulgare* and *Balkancar Holding*. Added to these commitments of the government should be the privatization of 20 small HPP, and the sale of at least half of the SMEs still remaining in state ownership. The letter to the World Bank expresses also the expectation of the privatization by the end of the year of *BTC EAD*. The commitments undertaken by the government are the condition for extension of the second tranche of the PAL loan.

In conclusion, it can be stated that in the first quarter of this year Bulgarian and foreign analysts again pointed out the issue of the prompt completion of large transactions as a major guarantee (or threat, respectively) for enhanced confidence of investors to the country. In their report of February¹² IMF finds that "the authorities need to speed up the completion of delayed privatization". "Though it is not critical from the financial point of view, completion of these transactions in a transparent way is a key to enhance the confidence of investors to the business climate".

¹¹ www.priv.government.bg

¹² <http://www.imf.org/external/pubs/ft/scr/2003/cr0332.pdf>

In the first quarter of 2003 the Agency for Small and Medium-sized Enterprises is seen to be more active in the area of encouraging the dialogue between the Government and small and medium-sized enterprises. The reason for such a conclusion is the **National Forum on the Problems of Small and Medium-sized Enterprises**, organized by ASME on 29 March. The problems of small and medium-sized enterprises were discussed at two more conferences during this quarter, namely **Lease Agreements - a Flexible Formula for Financing of Technological Renovation of Small and Medium-sized Enterprises in the context of their EU Accession**, a conference organized by the Bulgarian Industrial Association (BIA) on 24 March, and the **International Forum on the Issues of Small and Medium-sized Enterprises**, organized on 5 - 7 March by BIA with the support of the Union of German Chambers of Industry and Commerce (DIHK) and the project DIHK-ABC in cooperation with the Representation Office of German Economy in Bulgaria and the Bulgarian Chamber of Commerce and Industry. Some other important events in the area of small and medium-sized enterprises during this quarter were the **draft law on amendment to the Act on Small and Medium-sized Enterprises**, introduced into the Parliament on 25 February, the **new credit line received by ProCredit Bank from the Black Sea Bank for Trade and Development** for funding of micro, small and medium-sized enterprises in the country, as well as the **two new loan agreements between the Encouragement Bank and the Development Bank of the Council of Europe**, ratified by the Parliament, again in support to the small and medium-sized business.

By proposal of the government, the Agency for Small and Medium-sized Enterprises organized on 29 March a **National Forum for Development of Small and Medium-sized Business** where ministers, representatives of the business from all over the country, as well as representatives of the donor community took part. The goal of the forum was to achieve efficient interaction between the public administration developing the rules of the business environment and companies operating

in this environment in order to clearly identify the problems and impediments to the development of small and medium-sized enterprises in the country. The idea of the Government is that such forums turn into a regular event to play the role of a reliable tool to up-date the government policy and the program on SMEs. This forum was preceded by sending of proposals to the web-site of the Agency for Small and Medium-sized Enterprises for resolving the problems faced by representatives of the small and medium-sized businesses in the country. All proposals of the business were grouped in seven categories:

- Administrative and legal framework
- Funding and financial control
- Tax policy
- Social policy
- Regional policy
- Access to information
- Other

What is striking is that the proposals for resolving the problems of small and medium-sized business in the country are mainly in the area of tax policy, opportunities for funding and its legal regulation which proves that a targeted tax policy in support of small and medium-sized enterprises still lacks in Bulgaria and also points to the absence of an active government support to ensure guarantees for the collateral on loans required by banks for funding of projects of small and medium-sized businesses. Special attention was paid to the issues related to the introduction of information technology in support of small and medium-sized business, which proves that further actions are needed in this direction.

It was for the first time at this forum that the government categorically stated to the business community that a part of the collateral for lending will not be provided by a guarantee fund although its setting up was stipulated by the Act on Small and Medium-sized Enterprises. According to the President of the Agency for Small and Medium-sized Enterprises, the government and industrial organizations can provide another type of support to small and medium-sized business in the country by issuing written guarantees to companies with a

reputation of regular payers. Since the adopted Act on Small and Medium-sized Enterprises left unresolved the basic problem for the support of lending to small and medium-sized business in the country, a draft law was introduced in the Parliament on 25 February on amendments to the Act on Small and Medium-sized Enterprises and the proposals made in this draft are aimed to fill-in this gap in the legislation. The draft envisaged setting up of a Guarantee Fund with up to 51 per cent state participation to provide up to 50 per cent guaranteeing of collateral required by banks for lending to small and medium-sized enterprises, and thus the state can implement its policy in the area of encouraging the development of this business. In addition to specifying the role of the government in support to small and medium-sized business, setting up such a fund would be a successful measure to fight unemployment. It was made clear at the National Forum for Development of Small and Medium-sized Enterprises that there does not exist a political will to actively support small and medium-sized business in the country. The business community expected to hear about some new measures to limit gray economy, to decrease corruption and to raise employment levels, but this did not happen.

On 24 March the Bulgarian Industrial Association held a press-conference titled Lease Agreements - a Flexible Formula for Funding of Technological Renovation of Small and Medium-sized Enterprises in the Context of their EU Accession. Major emphasis was placed on the problems faced by small and medium-sized enterprises and the ways for their resolution, the leasing market and the advantages of lease financing. Lease financing possibilities are still not fully utilized by small and medium-sized enterprises for raising their competitiveness and this is due mainly to inadequate information with regard to the advantages offered by lease financing as an alternative to bank lending.

Problems of small and medium-sized enterprises were also discussed at the International Forum on the Issues of Small and Medium-sized Enterprises, which was a part of the 2003 program of the Working Group on Small and Medium-sized Enterprises to the

Bulgarian-German Cooperation Council. Participants in the work of the forum were representatives of government agencies, banking and financial institutions, business organizations, companies from Germany, Bulgaria and South-East European countries that have an interest and contribute to resolving the problems of small and medium-sized enterprises. The major topics discussed at the forum were the role of small and medium-sized enterprises in South-Eastern Europe, the German experience in supporting the sector, evaluation of the current cooperation between politics and economy in the countries of South-Eastern Europe and Germany in the area of SMEs, as well as proposals for basic points of a joint economic program of Germany and SEE countries in the area of SMEs for the next year. Studying foreign experience in support to small and medium-sized enterprises is without any doubt important, but in Bulgaria an active policy in support to small and medium-sized business which in fact is the basic source of employment in the country is still absent.

There are now two more sources for funding of small and medium-sized enterprises in the country with ProCredit Bank receiving from the Black Sea Bank for Trade and Development a credit line of EUR 6 m and the Parliament ratifying the framework loan agreements between the Development Bank of the Council of Europe and the Encouragement Bank AD at the amount of EUR 15 m. The credit line from the Black Sea Bank for Trade and Development will be used for the funding of micro, small and medium-sized enterprises, and this is the fifth credit line for ProCredit Bank. So far the bank has used EUR 5 m for lending, received from the US Government, USD 4 m from the International Financial Corporation (IFC), which is a part of the World Bank group, EUR 5 m from Kreditanstalt fuer Wiederaufbau (KfW) under the EU program and another EUR 4.1 m loan from the German Government. The loan agreements between the Development Bank of the Council of Europe and the Encouragement Bank ratified by the Parliament are expected to be used for funding of manufacturing and investment projects of SMEs under two programs of the Encouragement Bank AD: Long-term

Investment Financing of SMEs, and Improving the Competitiveness of Bulgarian Production. One of the agreements with the Development Bank of the Council of Europe amounting to EUR 10 m requires a state guarantee, while for the remaining EUR 5 m require only a Letter of Intent by the Ministry of Finance and this is the first credit line extended by the Development Bank of the Council of Europe to a Bulgarian bank without demanding a state guarantee which indicates a higher level of trust to the country and the banking system in particular.

Foreign Economic Relations

Trade data for the first quarter of 2003 are a positive surprise against the background of European economic recession and negligible US economic growth. The commodity structure of Bulgarian exports may seem inefficient, but it obviously has adequate potential in an environment of limited international market demand and reorientation of consumer demand from expensive high tech products to cheaper traditional goods. This may well explain the fact that in the first three months of 2003 **exported goods amounted to USD 1 709.2 m, registering a growth of 42.3 per cent** compared to the same period of 2002. The sizable change in the exchange rate within a year should be taken into account, but **even if the exchange rate influence is eliminated, growth remains notable – 19.2 per cent** (in BGN). Besides, the question is about estimates, which will be certainly adjusted, with real growth expected to exceed 20 per cent.

Imports (CIF) amounted to USD 2 190 m, registering increase of 39.1 per cent in USD and 16.4 per cent in BGN. Imports register smaller growth against exports, but that is not enough to decrease the negative balance. Registered **deficit amounts to around USD 500 m** (export FOB - import CIF) and remains some 35 per cent higher compared to the first quarter of 2002, but around the average quarterly level for the previous year.

Typical for trade dynamics is the higher growth of trade with OECD countries (the USA and Turkey), registering an increase of more than 56 per cent, and with non-aligned countries (China, Egypt, Brazil) where the increase is almost double. Despite that, **in terms of geographic structure, the EU continues to account for the highest share of 55.8 per cent in exports and 48.3 per cent in imports.** Italy, Germany and Greece preserve their top places and the corresponding share (more than 62 per cent) in the export of Bulgarian goods to the EU, followed for the first time by Belgium. In terms of imports, Germany leaves far behind all other European countries, which explains the traditionally negative balance of trade

with this country. Higher exports to OECD countries result in higher share of these countries in total Bulgarian exports - around 20 per cent. Their share in imports also increased, reaching 17.1 per cent. CEE countries preserve their share in trade (around 10 per cent), which is higher in exports (11.7 per cent) compared to imports (8.5 per cent). It is worth noting that Croatia is ranked for the first time among our traditional partners (Romania, Yugoslavia and Macedonia), with export to the amount of USD 23.8 m, registering increase of 400 per cent compared to the first quarter of 2002. This fact may be explainable by the signed free trade agreement, which took effect since 2002.

Notable positive trends are observed in terms of export commodities composition. Export of investment goods and of prime and raw materials registers accelerated growth (57.6 and 47.8 per cent, accordingly) compared to total exports (42.3 per cent). Thus the share of investment goods in exports increased from 13 per cent to 14.4 per cent within a year, and the share of raw materials increased from 40.4 per cent to about 42 per cent. Export of electrical machines and metals (ferrous and non-ferrous) registered particularly notable increased. Furniture and textile products registered the highest growth in the consumer goods group, which preserves its share of 35 per cent in total exports. In terms of imports, the four basic commodity groups (consumer goods, prime and raw materials, investment goods and energy resources) register almost equal growth (around 39 per cent), except for the prime and raw materials group (41 per cent), preserving their corresponding relative share of 35 per cent for prime and raw materials, 23 per cent for investment goods and 20 per cent for consumer goods

Efforts to improve the access of Bulgarian producers to foreign markets continued. **A free trade agreement was signed with Albania** in March. It will help facilitate trade and will contribute to its growth in the next months. The free trade agreement with Serbia and Montenegro has been negotiated and its signing is pending. It is expected to promote the trade between the two countries and to rank Serbia and

Montenegro first among Bulgaria's CEE partners.

Foreign Investments

In this quarter again, spoiled large privatization transactions did not justify expectations for higher inflow of foreign direct investments to Bulgaria. **Despite that, in the first quarter of 2003 the volume of foreign direct investments in Bulgaria (USD 181.5 m) registered an increase by USD 55 m (or 43.7 per cent) compared to the first quarter of 2002.** Given the absence of any proceeds from privatization transactions, the funds attracted from non-residents and the reserves of Bulgarian companies account for 56.6 per cent (or USD 102.7 m) of total investments for the period under review. The remaining USD 78.8 m come from operations with intercompany loans.

This means that **the companies which have entered on the Bulgarian market are operating and developing their business, attracting increasingly higher amount of funds from mother companies and foreign partners, but the economy remains in acute shortage of sizable green field investments and of sustainable inputs by strategic investors.**

The beginning of 2003 marked new preparatory actions by government authorities to place the Bulgarian energy sector on market foundations. The end result of these actions will support the improvement of competitiveness of energy intensive production operations and of the business climate in the energy sector and will assist easier adaptation of Bulgarian economic players to the European market. Passing of a law stipulating the obligations on maintenance of oil and oil products reserves will assist the negotiation process for Bulgaria's EU accession. A counter effect will have the unclear situation arising with regard to the validity of Bulgaria's commitment to close down units 3 and 4 of Kozloduy NPP in 2006.

State Policy

During the first quarter of this year the regulatory framework for the business actors in Bulgaria was complemented by the **Act on Obligatory Oil and Oil Products Reserves** in compliance with EU requirement that all Member States have available quantities of oil and oil products equal to their 90-day consumption. The objective is to avoid possible hardships in liquid fuel supplies with regard to the high level of dependence of European countries on external suppliers.

The Act delegates the monitoring on establishing and maintaining obligatory reserves of oil and oil products to the State Agency "State Reserves and Military Peace Time Reserves". The Agency is given the powers to determine the quantities each economic actor should maintain as an obligatory reserve, to define the technical requirements and safety requirements and to register storage facilities where reserves will be held, to control fulfillment of these obligations and, when necessary, to impose sanctions. The Agency is charged also with the responsibility to fix the reserves to be kept by the state.

The Act will have a direct impact on manufacturers and importers of automobile and aircraft petrol, industrial fuel, jet fuels of kerosene type and diesel fuel, heavy oil and LPG as they will have to organize and fund

themselves the establishment and maintenance of reserves in registered storage facilities. According to estimates of the Ministry of Economy the annual costs for the business from enforcement of the provisions of this law will amount at about BGN 160 m. Since these costs will finally be incorporated in the price of oil products, the costs of transport, chemical and energy companies will increase and this will result in higher prices of a wide range of goods and services for the end users.

To soften the financial effect, the law envisages the oil and oil product reserves to be gradually accumulated to reach the level of 90-day consumption for a period of nine years. Moreover, this process will commence at the beginning of 2004 so that the administrative capacity for its management to be built up. The law envisages gradual increase of the minimum number of days to be covered by available reserves and decrease of the relative share of the state in the quantity of reserves. The law requires that in the first year of introduction of obligatory reserves of oil and oil products a level of at least 10-day consumption volumes to be reached. The state will assume the organizational and financial responsibilities associated with this initial reserve accumulation.

In the first quarter of 2003 the Ministry of Energy and Energy Resources presented its **draft of a new energy law**.¹³ Its purpose is to regulate the public relations in the sectors of natural gas, electricity and heating power and to define the authorities of state bodies. The final draft, which was approved by the Council of Ministers in the middle of the second quarter, takes account of the recommendations made during the discussions with a broad range of experts and stakeholders. The need for new legislation arises from the changes in the energy sector that mark the start of establishment of a market-based model of relations in energy supplies.

Pursuant to the draft law the state policy in the energy sector will be implemented in accordance with

¹³ The text of the draft law can be found at the web-site of the Ministry of Energy and Energy Resources: www.doe.bg

a strategy to be approved by the Council of Ministers. The Ministry of Energy will play the leading role in the implementation of the energy policy. Decentralization of powers is envisaged through delegation to regional and local governments of duties and responsibilities related to projections, plans and programs for energy supply and management of local street lighting networks.

The Energy Regulatory Commission (ERC) is the body that will have a central role in the sector regulation. It is the successor of the State Energy Regulatory Commission (SERC). The draft law stipulates that ERC will perform the same functions that are now assigned to SERC. All existing formal requirements are also preserved aiming at a higher level of independence of the regulatory body like clearly formulated duties of the Commission, stated in advance requirements to the professional competence of commissioners, clearly defined duration of mandates and their overlapping.¹⁴ Added to these is a larger financial independence since the ERC budget will be now formed by the regulatory charges due by energy enterprises. The final draft law that was approved by the Council of Ministers in the beginning of May 2003 does not make it clear how deficits will be covered in case the funds raised from regulatory charges and donations do not suffice to cover the costs of ERC. Shortage of funds may prove to be a significant impediment to the normal functioning of the regulatory body and to result in low quality performance of the assigned duties that will in the end have strong negative effect on the energy sector, and hence, on the overall economy.

The draft law envisages that energy operations shall be subject to licensing. It revokes the now existing regime of permits for building up, expansion or decommissioning of energy facilities. The draft incorporates the idea that the state should take care of energy supplies security in the country, and the risks for the sale of excessive quantities in the country should be borne by the private sector.

Therefore, in case a need is established for a new generating capacity, ERC will hold a tender and the winner will be granted a license to build up and operate the respective energy facility. In the remaining cases a private investor will have to first build up the energy facility and only then receive the license for its operation. The draft law provides for keeping the monopoly in the transmission and regional distribution of electricity and natural gas and regional transmission of heating power, and introduces monopoly in public procurement and public supplies of electricity and natural gas.

Public suppliers and providers present a new category in Bulgarian energy legislation. These are the actors that will be responsible for the so-called universally provided service, i.e. for the transmission and supply of electricity and natural gas of fixed quality, regulated price and other agreed conditions, that can not be refused for reasons other than those stated in the law.

The draft law defines the powers and duties of the actors in the value added chain in supplies of electricity, heating power and natural gas and designs the framework for their commercial relations.

It is for the first time in the Bulgarian regulatory framework that a distinction is made between electricity traders and power system operators. This approach is required for the introduction of real market relations in the sector. The draft provides for electricity supplies to be made in a regulated or free market. ERC defines the rules of transactions in the regulated market. In the free market sellers and buyers can negotiate the conditions of supply through bilateral agreements or to take part in the so-called organized market. The organized market is a new form of trade relations in the Bulgarian energy sector and presents organized collection of offers for purchase and sale of electric power. The draft law envisages the issue of only one license for the organization of the market. The licensed entity will have the obligation to compare offers, to inform participants about available commercial opportunities and to fix the price of traded electricity for each period. The draft law provides

¹⁴ For more information, ref. the publication of the Center for Economic Development: Reforms in Electricity Sector and Their Impact on Consumers Protection (2002)

for keeping the monopoly on import and export of electricity until Bulgaria's accession as a full member to the European Union, and exclusive rights for supplies from and to foreign countries is given to the public supplier. Even after Bulgaria becomes an EU member there will be no full liberalization of electricity trade since non-eligible consumers will not have the right to import. In addition, the range of foreign trade partners will include entities from EU and countries, with which Bulgaria has concluded an agreement for joint application of the EU law, that are entitled to trade freely with electricity.

The present organization of the relations is preserved in the heating power sector between generators, heat transmission operators, enterprises for heating share distribution in condominium buildings and end-users. A novelty presents the provided opportunities for household users in condominiums to unite in an association and thus enter in contractual relations with the heating supplier with regard to the heating supply. Associations will be constituted under the Act on Non-for-profit Legal Entities. The draft law itself introduced provisions related to the setting up, management, operation and termination of associations. In order to encourage the establishment of such legal entities the draft law envisages that they will pay for the consumed heating power at preferential prices. The existence of associations of users in condominiums will, no doubt, facilitate the operations of energy companies, as it will save the numerous problems with individual users. From the consumers' point of view, however, the constitution, management and operation of such an association require significant efforts. Financial and non-financial costs related to these activities may in the end neutralize the benefits of lower prices, and thus limit the establishment of such associations in the years to come.

The increase of green energy as a means to guarantee the security of supplies and the quality of life is among the leading EU goals in the area of energy. By Directive 2001/77/EC¹⁵ the European Union requires that Member States undertake active measures to encourage the use of renewable sources and sets two indicative targets of their share in the total

production of electricity for each country: 12 per cent in 2010 and 22.1 per cent in 2020. Taking into account these targets the Bulgarian draft law provides for a preferential regime for renewable energy sources and combined generation of electricity and heating power. In the short-term it will replicate the now existing regime of priority purchasing at preferential prices of electricity. In the longer term the draft law envisages the introduction of a system of issue and trade in green certificates. Within this system the minister of energy will determine the minimum obligatory share of electricity produced from renewable energy sources or through the combined method, in the output of each producer. In case the latter is not in the position to ensure independently such an output, it can meet the requirement by buying a green certificate.

The draft law proposes a regulation of the gas market in which extraction companies, traders and eligible consumers will have the right to conclude contracts among each other and negotiate independently the terms and conditions of supply. Parallel to this the draft requires that these conclude also deals with the transmission company to ensure balancing of the market.¹⁶ All remaining deals for natural gas supplies will be conducted within the regulated market under conditions approved in advance by ERC. The draft law provides for liberalization of natural gas import and gives an opportunity for traders and eligible consumers to conclude independent contracts with suppliers from abroad. Extraction companies will be able to independently export natural gas for foreign customers but only if they construct their own pipelines to them.

Unlike the current situation, the new energy legislation will comprise two separate laws on public relations and energy efficiency. The draft of the second one has still not been exposed for public discussion. The law on energy efficiency will be the basic statutory instrument for targeted support to a

¹⁵ Directive 2001/77/C of the European Parliament and of the Council of 27 September 2001 on the promotion of electricity produced from renewable energy sources in the internal electricity market http://europe.eu.int/eur-lex/prl/en/oj/dat/2001/1_283_28320011027en00330040.pdf

¹⁶ Balancing of the market means organized trading in natural gas for the purposes of maintaining a balance between import/generation and consumption of the fuel.

more reasonable use of energy resources. The delay in its passing and enforcement will not be of use to overcome the extremely irrational management and use of energy resources in the Bulgarian economy and the household sector thus impeding national competitiveness.

During the quarter under review Bulgaria fell into an **unclear situation concerning the future of units 3 and 4 of Kozloduy NPP**. It emerged when in the beginning of the year the Supreme Administrative Court repealed Decision No. 641 of 1 October 2002 of the Council of Ministers in the part approving additional information to the position in the EU negotiations on the Energy chapter. The repealed text states that Bulgaria accepts the Common position of EU on the closure of units 3 and 4 of Kozloduy NPP and takes the commitment to close these down by 2006. Following an appeal by the ministers of energy and foreign affairs and the minister of European affairs and chief negotiator, a five-member panel of the court reconfirmed the initial court judgment. Thus a contradiction was created between the lawfulness of the decision on closing down the two units on the one hand, and the commitment of the government to EU, on the other hand. This case has still not been clearly and reasonably resolved. Seeking such a solution the Council of Ministers set up in the middle of the second quarter a working group headed by the minister of energy, which should propose by the end of June a strategy on the progress of negotiations with EU with regard to the created situation.

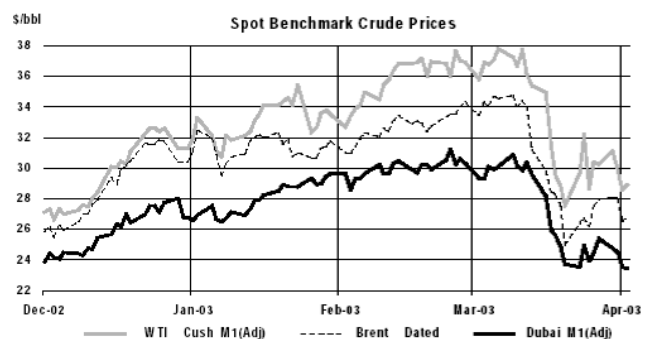
At the end of the quarter the **State Energy Regulatory Commission invited 10 companies to declare their interest in acquiring the status of an eligible consumer** in compliance with the Ordinance on the Access of Eligible Consumers and Independent Power Producers to Electricity Transmission and Distribution Networks. Thus, the first real step is made towards the opening-up of the internal electricity market and the creating of a competitive environment in electricity supplies. The group of potential eligible consumers includes: Mini Maritza Iztok EAD, Stomana Industry AD, KCM (Non-ferrous Metals Combine Works) AD, Assarel Medet

AD, Elatzite Med AD, Umicor Med AD, Devnia Cement AD, Lukoil Neftochim Burgas AD, Agropolychim AD and Neochim AD. These are mainly companies that are both large electricity consumers and leading Bulgarian exporters. Provided that they manage to negotiate with independent producers better terms and conditions of supplies, such an initial liberalization of the electricity market may have a considerably favorable impact on their competitiveness. The favorable effect will be multiplied by the fact that a part of these companies are vertically linked. There will be positive consequences for the industry competitiveness in the extraction and processing of non-ferrous metals and the chemical industry, as the ten potential eligible consumers include several significant representatives of these sectors.

Energy Prices

In the first quarter of the year crude oil quotations on the world markets remained unstable. In March they reached a 12-year peak and then marked a substantial drop down. Their dynamics was mainly determined by the tension around Iraq and expectations for military actions in the country which has the second world largest oil deposits. Recovery of the production in Venezuela, increased supplies from the OPEC countries, of the oil reserves and climatic changes in the USA were some additional factors of considerable influence on the dynamics of crude oil prices during the quarter under review (Figure 14).

Figure 14. Dynamics of crude oil spot prices - WTI, Brent and Dubai



Source: Monthly report on crude oil prices, International Energy Agency, April 2003., <http://www.iea.org/omrep/10apr03pri.pdf>

Meeting 99 per cent of its needs of crude oil through import under conditions following the international situation, the Bulgarian economy experienced the effect of unstable quotations on the world markets. Fuel prices on the domestic market jumped up. The effect of higher levels of oil product prices was softened by the declining exchange rate of the US dollar over the quarter. Higher fuel prices had the strongest impact on the transport sector, and because of the permanently high levels of fuel prices transport operators raised the prices of their services, thus transferring additional costs onto their customers.

The upward trend of oil product prices on the world markets during the last months was also reflected in the natural gas price for Bulgarian consumers. Over the last six months the marginal prices of Bulgargaz EAD supplies had not been changed, but as of the beginning of April these were increased by 2.5 per cent on average for clients connected to the transmission and distribution networks of the company. The small change in the price, to which the lower USD/BGN exchange rate contributed, will not result in substantial increase of natural gas costs for users. It will not significantly harm heating companies, since they have minimum levels of generation in the spring and summer season.

In view of the started decline in oil product quotations at the end of the quarter and the ongoing drop of the exchange rate of the US dollar to the Bulgarian lev, it could be expected that in the second quarter of 2003 Bulgarian users' costs for oil and oil products will go down. An adjustment in the price of Bulgargaz EAD for natural gas supplies to the domestic market may be expected at the beginning of the second half of the year at the earliest, when ERC will have the right to revise prices. Changes in natural gas prices will be smoother since they account for the dynamics of prices of heavy oil and gas oil, demand and exchange rates over a longer retrospective period.

In the first quarter of 2003 the transport sector did not witness any developments, which to improve either the efficiency of the sector or the benefits its services generate to other sectors.

The beginning of the year did not bring changes in the corporate structure of the railway transport.

The lack of a flexible approach in the business relations with customers on the part of the state monopolist BDZ may prove a catalyst for the entry of new shippers-established carriers. The most outstanding example of such behavior in the period under review was the conflict between the state railway carrier and Kremikovtzi about the one-sided 40 per cent raise in the transportation fee. Such an act lowers the shipper's price competitiveness and undermines its market positions. If the intentions of the metallurgical company come true, BDZ will lose one of its biggest customers, as Kremikovtzi accounts for around 25–30 per cent of the cargo and around 12 per cent of the carrier's income. Cargo loss will create financial problems for BDZ because the cargo transportation, unlike passengers transportation, is a profitable business for the company.

The new national air carrier Bulgaria Air (the name was chosen by the Ministry of Transport and Communications /MTC/ after a national public opinion poll) **continues to enjoy strong government support.** The measures to promote company development include, among the others, the granting of the right to fly to new destinations and the rejecting of the requests of private carriers to serve regular destinations, which Bulgaria Air does not fly to. Despite the positive signals for more passengers compared to the initial projections, in the first quarter of 2003 the company continued to generate significant losses, amounting to BGN 2.117 m, compared to projected BGN 2.068 m. The negative financial situation is a result of: the continuing low confidence of passengers in the quality of services offered by the national carrier, its commitment to carry passengers against tickets issued by the bankrupt Balkan Airways, the lower traffic and the higher fuel prices as a consequence of the Iraqi crisis.

It is at this condition of the national air carrier that the preparation for its privatization was started.

The amendments to the Privatization and Post-privatization Control Act placed the company on the list of enterprises of importance for the national security. Consequently, if over 50 per cent of its capital are sold, the decision on the buyer shall be taken by the Council of Ministers and shall be approved by the Parliament. Only one candidate submitted an offer in the tender for a consultant on the privatization of the national air carrier - the Central Cooperative Bank - Deloitte & Touche Consortium. It was appointed consultant and has the task to carry out the marketing activities, to provide general consulting to the Privatization Agency, and to assist the latter in preparation of the sale. There is still lack of clarity about the share of the capital to be offered for privatization. MTC insists that the State should keep a share of 51 per cent, because the carrier appointed under bilateral agreements must have not less than 51 per cent Bulgarian participation in the capital. Another argument of MTC is that thereby the problems, which appeared in the post-privatization development of Balkan Airways, will be avoided. Studies conducted by the Privatization Agency reveal, however, that such a scheme will not attract quality investors.

The privatization of Bulgaria Air was started in a very difficult period for the whole aviation business. The first clear indications of stagnation in the sector were registered in the autumn of 2000. The attacks of 11 September 2001 caused significant damage to the sector, generating the biggest financial loss, which are estimated by the International Air Transport Agency at USD 18 billion, and a loss of more than 200 000 jobs. There was some stabilization in 2002 and even European air carriers reported better results in terms of the occupied seats and passenger-kilometers indicators. Expectations about military actions in Iraq and the 2003 war itself had further negative effect on almost all companies. Conflict-generated losses for the aviation business are estimated at more than USD 4 billion. Lower travelers' interest in air services was registered in recent months as a result of canceled flights, mainly to Asiatic countries

on account of atypical pneumonia dissemination. The impact of these events made leading North American companies seek the protection of the law to defend themselves from creditors, and European governments as well as the US government think about financial aid to support the air carriers in their countries. Global rating agencies stated in connection with the crisis that they would probably lower the credit ratings of more than 10 air carriers.

The inferior competitive position of Bulgaria's national carrier should be added to the unfavorable international environment in which its privatization was started. As a result of the problems that Balkan Airlines had for a couple of years, foreign airline companies have occupied the air traffic niche from and to Bulgaria. The major current advantage of Bulgaria Air is the right of carrier under bilateral agreements. The European Open Sky Agreement will neutralize this advantage because it will allow all carriers to fly freely to all destinations since 2005. Bulgaria will probably sign the agreement in June 2003, but MTC is still reflecting on the opportunity to request a transitional period for its implementation in order to protect the Bulgarian aviation sector and the current national carrier in the first place.

The combination of the poor and unstable yet competitiveness of the national company and the unfavorable situation on the international aviation market may prove a serious obstacle to finding quality investors for Bulgaria Air and for the success of the privatization procedure, accordingly.

Despite the harmony in the opinions of the Executive and the Legislature about the need and the benefits of the entry of private operators in the management of ports and airports, no significant progress was achieved in that respect. The slow pace of the parliamentary discussion on the amendments to maritime transport legislation, the differences in the opinions about the particular concessioning mechanisms, and the need for reopening of due diligence procedures for of a couple of ports and terminals constitute barriers to a faster concessioning. At the same time, most ports and

airports reported better results in terms of passenger and cargo traffic and higher financial income for 2002 compared to the previous years. Improved physical infrastructure and management thereof, with a view to satisfy the needs of both shippers and carriers is a prerequisite for making this positive result a sustainable trend. That requires significant investments and know-how for performance in a competitive environment, which are more typical for the private sector.

Some progress in the construction of Bulgaria's large transport infrastructure projects was achieved in the quarter under review. The construction works of a new passenger terminal at Sofia Airport (Lot B1) started in the middle of the period, and later the contract for the construction works under the project for building a new runway to be put into operation in early 2005 (Lot B2) was signed. The implementation of the two projects will result in improvement of the Bulgaria's general aviation infrastructure, in opportunities to attract more travelers at higher service standard, and in creating better opportunities for tourism and business development. The new runway will help to lower the noise level in adjoining Sofia quarters, thereby contributing to improved quality of life. Favorable economic effects for Bulgaria will be felt as early as the projects implementation phase through the participation of local labor and local companies in the construction works and in the supply of materials and equipment.

The first three months of 2003 did not bring the desired positive development of some acute problems of Bulgaria's information and communication technology market (ICT) - the privatization of BTC, and the draft law on Telecommunications are a most outstanding example in this respect. Nevertheless, during the period the tendency towards revival in the sector continued.

Changes in the situation with Bulgarian Internet providers were observed in early 2003. In January the Greek company PROMOTA HELLAS bought the whole block of shares of a major market actor – BITEK.COM. PROMOTA HELLAS is listed on the Athens stock exchange and is among the 500 most rapidly developing companies in the European Union. In addition to BITEK.COM, PROMOTA HELLAS also invested more than EUR 7 m in a couple of other projects in Bulgaria.

Revival of the market of alternative telecommunication services via Internet (Voice over Internet Protocol or VoIP) was also observed in early 2003. Some major market actors in this segment of the telecommunications sector announced serious cut down of call prices. At the same time, there is not yet real assessment of the VoIP market volume; experts share the opinion that it accounts for around 2 per cent of BTC's traffic. It is only logical to expect increase of this share in the near future, given that after elimination of BTC's monopoly alternative operators may supply their own VoIP service with a delay of less than 250 milliseconds, which will attract increasingly higher number of new customers.

A Strategy for Development of Electronics and Electrotechnology in Bulgaria was prepared in February. The purpose of this document is to serve as a "road map" for development of the sector and to outline its basic priorities and challenges. The Strategy was developed by the Bulgarian Chamber of Electrotechnology and BIC Capital Market EOOD with the financial support of the German Society for Technical Cooperation (GTZ).

The paper contains a detailed set of recommendations

for reforms towards the Government, the basic business institutions, and the companies. It comprises proposals covering different spheres like public financing, corporate financing, information technologies, transport, education, optimization of market or production lines at company level. According to experts, the Strategy cannot be an ultimate goal; it is only an initial step to make electrotechnology a competitive Bulgarian sector providing permanent skilled employment. To achieve this goal, it is of vital importance for the State to cooperate with the business, with a view to create together the necessary organization for development and implementation of specific programs and measures.

A draft law on the Use of Free Software in the Administration was introduced in the National Assembly at the end of March. The purpose of this draft law is to create adequate environment for successful citizens - government administration cooperation via Internet. The draft introduced in parliament proposes detailed definition of the organizations, which in the opinion of the authors must be obligated to use free software and open formats in their information systems (IS). Some of the most important organizations include: government authorities, mayors of municipalities and districts, higher education schools, medical establishments, non-profit legal persons, as well as other authorities and persons which dispose of funds from the state or municipal budgets and/or off-budget accounts or funds, NSSI, NHIF, diplomatic and consular representations, state-owned enterprises and commercial companies with more than 50 per cent state participation. The draft law also gives definitions of the notions computer IS, software, user, free software (free computer program), open format, etc. The positive aspects of free software (FS) in terms of national security protection, technological independence and lower software costs¹⁷ are pointed out as a major advantage of the adoption of such act. It is true that many European countries as well as some of the United States give strong support to the

¹⁷ For more detailed information on the advantages of the use of FS in government administration see the motives to the draft law (<http://www.parliament.bg/infocenter/zakonoproekti/354-01-17.pdf>)

use of FS in government administration, and Bulgaria should also take steps to that effect. Bulgarian non-government organizations already work along these lines. The Open Source Software for Bulgarian Non-Government Organizations Project¹⁸ was launched in February 2003. It is lead by the Red House Center for Culture and Debate and the Interspace Center for Media Arts. The purpose of this initiative is to promote the use of these software products in Bulgarian NGOs. There is, however, a hidden problem, which is often neglected in the euphoria to introduce FS. It is related to the more difficult and expensive provision of specialists to maintain FS in organizations with complex ISs. That is why, the organizers provide under the above project a period of two years with free maintenance and training in the new programs for NGO's personnel.

The initial step towards elimination of BTC's monopoly in the telecommunications sector was taken in the first quarter of 2003 - Orbitel, one of the biggest Internet providers, filed an application for a telephone operator's license to the Telecommunications Regulation Commission. At this stage real competition with BTC is unimaginable and impossible, but nevertheless, such actions signal positive development of the sector in Bulgaria, and the announced similar intentions of other companies are another proof of the viability of companies in the telecommunications sector.

The first quarter of 2003 did not bring the long-expected conclusion of BTC's privatization, either. A series of scandals about the ownership and origin of the approved candidate Viva Ventures, the telecom's 2002 profit distribution, the draft law on Telecommunications, and the opportunities to grant a license for a third GSM operator were but a few of the events around the long-expected privatization in these three months. Meanwhile BTC reported 2002 earnings to the amount of BGN 1 025 837 000 and a 8.8 per cent growth compared to 2001. The accounting profit for the previous year is BGN 263.163 m (an annual growth of 4.4 per cent). The balance-sheet or the net profit amounts to BGN 198.963 m, registering a growth of 13.1 compared to 2001.

Similar to the privatization of BTC, the passing of the new draft law on Telecommunications did not become a fact in the first three months of 2003. The Ministry of Transport and Communications made sizable corrections in the document before its introduction in parliament for second reading, but nevertheless the act was not voted by the end of March. Corrections took account of the notes of the Commission on European Integration, of some conditions laid down by the potential buyer of BTC, and of recommendations by experts in the sector.

A new Deputy-minister of Transport and Communications in charge of ICT development was appointed with great delay in March. The post was taken by a financial expert with serious career in the banking sector, but without any previous contact with the problems and opportunities of this constantly and rapidly changing economic sphere. Yet the very act of appointment is indicative of Government's intentions to formulate a policy on improvement of the situation in the sector.

The data given in the next two tables and provided by the national card operator BORICA are not less interesting. The number of issued cards and service devices (automatic teller machines and POS terminals, Table 9) register apparent growth. These facts are extremely important in view of the growth of potential e-trade users in Bulgaria. On one hand, customers increase, and on the other hand, companies, which want to invest in such initiative, are able to place advanced technologies at the service of their business. The second table (Table 10) contains data about transactions via Internet, ATM and telephone for the whole 2002 and for the first quarter of 2003. It reveals that Bulgarians obviously begin to make more extensive use of the advantages of card settlements, which indicates positive attitude towards ICT in the country.

¹⁸ Accessible at: http://www.redhouse-sofia.org/bg/projects/c_opensource.html

Table 9. Automatic teller machines, POS terminals, and bank cards

| Installed automatic teller machines, POS terminals, and bank cards issued | 31.12.2002 | 01.04.2003 | Growth for the first quarter |
|---|------------|------------|------------------------------|
| Total installed automatic teller machines | 829 | 912 | 10% |
| Total installed POS terminals | 2 554 | 2 728 | 7% |
| Total bank cards issued | 1 614 105 | 1 802 675 | 12% |

Source: BORICA, www.borica.bg

Table 10. Transactions via Internet, ATM and telephone

| Total transactions for the period | 2002 | 2003, first quarter |
|--|--------------|---------------------|
| Total transactions via Internet (ePay.bg system) | 36 441 | 11 557 |
| Total payment of services transactions via ATM | 35 071 | 18 619 |
| Total payment of services transactions via telephone | 12 018 | 3 320 |
| Total amount, transactions in BGN for the period | 2002 | 2003, first quarter |
| Total amount, payments via Internet | 1 608 733,11 | 601 579,77 |
| Total amount, payment of services via ATM | 1 116 858,19 | 676 923,72 |
| Total amount, payment of services via telephone | 423 876,96 | 168 608,11 |

Source: BORICA, www.borica.bg

The data in the two tables, along with IDG's information about **2002 Bulgarian computer market volume**, give grounds for positive expectations about higher ICT consumption in Bulgaria. According to IDG - Bulgaria's survey, the growth registered in the fourth quarter of 2002 is 52 per cent compared to the same period of 2001 and nearly 62.8 per cent compared to the third quarter of 2002 (data cover the market of notebooks and desktop PCs and servers). This serious year-end growth is explainable by the fact that in the last months of the calendar year companies and government administration usually accelerate their activity and utilize planned budgets which have not been earlier expended.

It is true that not all expectations and wishes for a favorable environment for development of high technology and communications in Bulgaria are fulfilled, but overall the sector moves forward and is increasingly making use of its full potential. However, the passing of the new Telecommunications Act and the successful privatization of BTC remain the best opportunity to accelerate positive changes and confirm growth trends.

Number of Tourists and Revenues from Tourism

Two events in the first quarter of 2003 have negative effect on global tourism development. The war in Iraq and the atypical pneumonia epidemic resulted in material cut down of global travels, including tourist visits.

As early as the start of military actions the Global Council on Travels and Tourism prepared two scenarios for tourist industry development - in the event of a brief military operation and of long military actions. Both scenarios envisaged lower number of travels and lower revenues from tourism, as well as material cut down of jobs in the tourist sector and of flights. The atypical pneumonia epidemic is expected to have particularly negative effects on the economy and on tourism.

In the quarter under review these negative factors did not have such significant effect on Bulgaria. **Higher revenues from tourism prove that - in the first three months they reached USD 172.3 m, registering an increase of about USD 20 m compared to the same quarter of 2002.** Revenues registered in the three winter months are higher compared to the same period of 2002, exceeding USD 60 m in March alone.

Bulgarians' spending on travels abroad also registered an increase, reaching USD 136 m for the first quarter of 2003, with USD 120 for the period January - March 2002. **In the first quarter of 2003 net revenues from tourism amount to USD 35.7 m, compared to USD 32 m for the first quarter of 2002.**

Environment for Development of Tourism

The winter season was a success owing also to the good meteorological conditions - favorable temperatures and snow on the tracks of winter resorts. Implemented measures to develop infrastructure, as well as the united efforts of tour operators, hoteliers and owners of ski lifts in Borovetz and Bansko, also contributed to a **longer winter season**.

In the first quarter Pamporovo also produced good examples of partnership in solving common problems.

Pamporovo 2003 Joint-stock Company was set up in the resort in February. The idea is to establish the Pamporovo trademark as a whole, to ensure joint participation in international tourist exchanges, organization of folk festivals, ski competitions, general personnel training. Large-scale investment programs have been announced to improve the infrastructure. Short-term plans envisage construction of artificial snow installation and night-time track lighting, as well as a lift on the northern slope towards Stoykite. The objective of the long-term project is to build lifts connecting the tracks of Pamporovo and Chepelare.

World's biggest and most prestigious tourist exchange was organized in Berlin in March. This is the most important event for Bulgaria's tourist industry in the preparation of the coming summer season. A number of Bulgarian companies as well as representatives of the Ministry of Economy took part in this forum. It was noted that global events generate material cut down of registrations for travels to a number of traditional destinations like Turkey, Spain, Portugal, Tunisia, Egypt, and Morocco. Registrations for some other destinations register a standstill. Notes on Bulgaria reveal that at this stage the above events do not have negative effect on preparations for the summer season and expectations about sea holidays are optimistic. Summer registrations of German tourists register 10-per cent growth compared to the previous year. All big German tourist operators like TUI, ITC and Thomas Cook register similar growth. These companies plan investments in reconstruction and rehabilitation of Bulgarian hotels. Thomas Cook, for example, plans to set up a special fund of EUR 100 m to be appropriated for reconstruction of 15 Bulgarian hotels.

Tour operators project growth of summer holiday registrations on the last minute travel principle in the early summer season. This is particularly true for tourists from Germany and the other West European countries.

Government's decision to **cut down three times**

visa prices for nationals of Russia, Ukraine, and Byelorussia (taken in the first half of April) will have a positive effect on tourists flow, especially in the summer seasons. Until now, they paid USD 55 per visa, and after the decision they will have to pay USD 20. Reduction will be valid till April 2004. Government's decision was provoked by the notable drop down in the number of tourists from the above states in the previous year, which was also a result of the introduced visas. A decision for temporary elimination of short-stay visas for tourist groups from Latvia, Estonia and Lithuania was also approved.

The Agency for National Advertising and Information has not been formally set up yet, despite the fact that it had to be established as early as the end of 2002 when the new Tourism Act took effect. **The draft national advertising budget discussed in the National Council for Tourism includes an amount of USD 4.5 m.** Expectations pointed to a sum of USD 20 m, and despite the fact that the amount is twice higher compared to the previous year (about USD 2m), budgeted resources are insufficient. It is true that the amount is small compared to our major competitors - Turkey, for example, will budget around USD 65 m for national advertising in 2003. Besides, it is extremely important what funds will be spent for and whether in a transparent way.

The resources are allocated for publication of advertising materials in foreign media (Germany, Great Britain, Russia and Ukraine in the first place), organization of Days of Bulgaria and tourist presentations, for publicity brochures and billboards, as well as for marketing surveys, analyses and forecasts. The set up of a national tourist information system and the publication of an album on Bulgaria in English, German, French and Bulgarian will be an important item in the budget. There is a need to unite the efforts of the State and private entrepreneurs in promoting Bulgaria as an attractive tourist destination.

The launch of a Development of Cultural Tourism in Bulgaria Program, to be financed under the PHARE Program, was announced in the first quarter

of 2003. Program funds amount to EUR 6.6 m, to be provided in the form of subsidies for projects with value from EUR 50 000 to EUR 350 000. The project targets regions, municipalities and non-government organizations. Proposals must comply with regional development programs. The objective is to promote the development of cultural tourism, the rehabilitation of cultural monuments, to improve the marketing of cultural tourism products on the domestic and the foreign market, etc.

Condition of the Sector

Officially first quarter data on the share of the agricultural sector in Bulgarian economy are not available yet. Taking into account the continuing downward trend and seasonal specifics, one could estimate that in the quarter under review agriculture accounts for 7.6 per cent of GVA and 6.4 per cent of GDP. A revival on the land market is observed, characterized by higher number of sale transactions, higher average price and improved tenancy relations. An incentive of around BGN 10 per decare is set up for estates, which have not been cultivated for minimum three years, with a view to decrease uncultivated land. The funds shall be allocated from the Agriculture State Fund.

As a result of the unfavorable weather conditions some of the winter wheat sown froze and there will be a need to put the areas under spring wheat. The areas under winter wheat (around 11 m decares) are less compared to a year earlier and about 8 to 10 per cent were seriously damaged by frost (particularly those in Northeast Bulgaria). Despite that, higher yields could be expected as farmers were subsidized to buy quality seeds, fertilizers and diesel fuel. The Ministry of Agriculture expects wheat yield of around 2.5-2.7 m tons. Despite the slight delay in the pace of grain export in early January, projections show that some 350 thousand tons will be exported until the new crop (that is, in the first two quarters of the year), whereby total export of grain crop 2002 will exceed 1 m tons at an average export price of USD 100 per ton. The quantities bought by the Grain State Fund set up in mid-2002 are selling well and the last lots are expected to be sold by the end of the second quarter, exceeding the amount of invested funds.

Project financing under SAPARD continued at accelerated pace - 100 new projects amounting to a total of BGN 81 m were approved in the first quarter of 2003 alone. The highest number of approved projects comes under measure 01 – investments in farms. There is growing interest towards development of processing and marketing improvement projects (particularly in the local sector). Projects in the

apiculture, rural tourism, herbs and mushrooms processing sectors increase.

Environment for Development

The **pilot census of farms** in 28 land territories of all Bulgarian regions started on 26 March¹⁹. The objective is to test the method of the regular census to be taken in the period 1 July - 30 November 2003. The basic task is to update available data about the number of farms by regions, the area of cultivated land, the number of animals bred, the output volume and the number of employed in the sector. Census data shall be entered in the EU database and shall be a major instrument to protect Bulgaria's positions in the negotiation process, because they will be the basis to grant agricultural support subsidies after the country's accession to the Community. This census will help fully harmonize Bulgarian agricultural statistics with that in the EU.

Improvement of the mechanisms to support agricultural production by way of state subsidies and by **promoting the association of agricultural producers** continued. Amendments were introduced to Ordinance No. 15/2001 on the Terms and Procedure for Providing Financial Grant for Development and Diversification of Economic Activities, Providing Opportunities for Multilateral Activities and Alternative Income under EU Special Pre-accession Program for Development of Agriculture and Bulgarian Rural Regions. Association of agricultural producers is promoted with a view to improve the quality of agricultural production and make it more attractive for processors.

Financial resource of BGN 210 m is allocated for 2003 from the Agriculture State Fund, BGN 40 m whereof are envisaged for **direct support of producers**. BGN 70 m are allocated for the Fund's investment programs (Plant-growing, Stockbreeding, Agricultural Equipment). Farmers will receive additional subsidies for cultivation of different agricultural crops from the

¹⁹ The Act on the 2003 Census of Farms in the Republic of Bulgaria was promulgated in Official Gazette, No. 17/21.2.2003

corresponding Fund's lines. An annual subsidy of BGN 9.5 m is allocated for wheat production. A credit of BGN 8 m is also provided. The subsidy amount is higher than the credit amount on account of the stage-by-stage implementation of the European mechanisms of support by direct payments instead of credits. For the first time agricultural producers will receive before harvest-time a subsidy of BGN 1 per decare for a total of 2.5 m decare. The State will continue to support the farmers who store wheat in licensed corn houses. The direct subsidy allocated for this purpose amounts to BGN 1 m. Another BGN 6 m are allocated for the autumn sowing of crop 2004. BGN 1 m of that amount are allocated for seed production, BGN 2 m - for fertilizers, and BGN 3 m - for purchase of quality seeds. BGN 2 m are allocated for financial support of vegetable production through the Agriculture State Fund. Vegetable production is declared a priority area of financing through the fund.

At the end of March the Managing Board of the Tobacco Fund and the Council of Ministers adopted a **National Strategy for Development of Bulgarian Tobacco Growing till 2007**, which was worked out on the basis of the Tobacco and Tobacco Products Act and the Rules on its implementation. The Strategy also takes account of the adopted provisions for enforcement of EU Common Agricultural Policy in the sector. Having in view the social and economic importance of the tobacco-growing sector, the National Strategy aims to:

- improve the national balance of payments by building up a resource for export of tobacco and tobacco products;
- guarantee employment and certain income level for the population of mountain and hilly regions;
- balance the interests of all tobacco sector subjects - producers and traders of raw and industrially processed tobacco.

Tobacco competitiveness will be improved by way of keeping the level of minimum purchase prices with parallel raise of the premium for tobacco producers, as well as through stage-by-stage increase of targeted monetary support. Major priorities of

National Strategy implementation include structural improvement and promotion of the development of export oriented tobacco brands, as well as preservation of the environmental purity of Bulgarian tobaccos. The Strategy sets the following objectives to be achieved by the time of Bulgaria's accession to the EU: Bulgarian raw tobacco production should reach 77 000 tons, the average annual export of Bulgarian tobaccos – 45 000 tons, and national cigarette production – 30 000 tons. Minimum tobacco purchase prices will be determined, as hereto, on the basis of production costs, international tobacco prices and Government's opportunities to grant bonuses. The Strategy has been developed at an average annual exchange rate of BGN 2 per US Dollar and average annual inflation rate of 4 per cent. Should there be changes in currency values and the inflation rate, the National Strategy can be adjusted accordingly.

The Ministry of Agriculture and Forestry has worked out a Strategy for Development of the Vine-and-wine Sector, which envisages that the Agriculture State Fund shall open a financial line for grant aid of BGN 100 per decare of new vines. Priority measures in the sector include: vine lands consolidation and establishment of a reliable and express system to inform producers about financial resources; replanting and uprooting 40 000 decare of vines; financing the formation of tracts of land for production of propagating material. The orientation of the vine-and-wine sector towards European market requirements will contribute to its accelerated development.

Some positive trends from 2002 continued in the first quarter of 2003 – stock exchange trading in compensatory instruments, after its start in the last fall, preserved its level of activity, the SOFIX index was increasing over most of the period and at the same time market capitalization grew over the three months.

Nevertheless, the role of the capital market in Bulgaria's financial sector remains insignificant – at the end of March 2003 the total market capitalization of Bulgarian Stock Exchange – Sofia AD is a little above 4 per cent of the up-dated projections (source: IMF) of GDP for 2003. Underdevelopment of the capital market is to be explained by both the condition and prospects of Bulgarian economy as a whole and the circumstance that the financing mechanisms through such an alternative non-banking environment remain unknown or non-preferred even with the availability of relevant projects. **Liquidity remains low, the market does not encourage good practices of corporate governance and investment alternatives remain limited.** Financial intermediation is still provided mainly through the banking sector.

The capital market through the indicators of Bulgarian Stock Exchange – Sofia AD (without the compensatory instruments market)

As of 31 March 2003 the market capitalization according to data from the stock exchange amounted to a total of BGN 1 426 888 968 (out of which BGN 242 948 638 on the official markets) while at the end of 2002 market capitalization totaled BGN 1 375 184 361 (out of which BGN 252 873 237 on official markets). Turnover in the first quarter of 2003 is BGN 59 182 744 with 11 444 989 traded securities (this turnover and traded volumes do not include compensatory instruments and rights traded on the stock exchange, but include block transactions, again excluding compensatory instruments). This presents a decline compared to the previous quarter. The SOFIX index continued its upward trend but after the mid of March it suffered a correction. Yet, as of 31 March SOFIX value was 229.14 while 2002 ended

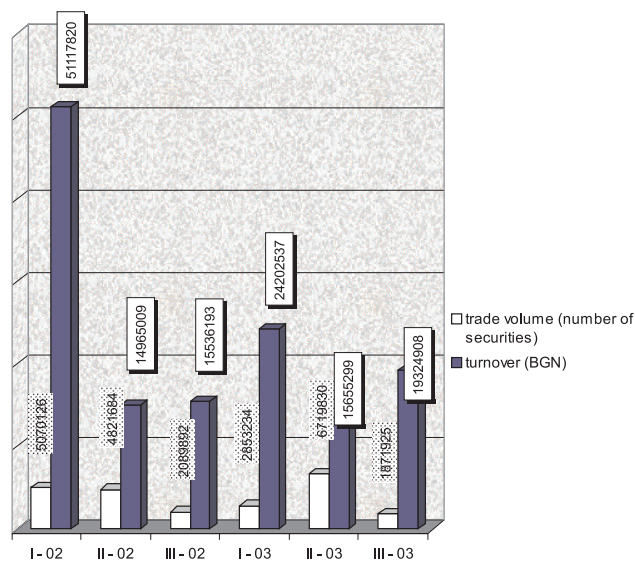
at 183.08, and a year ago, i.e. 31 March 2002, it was 120.56.

Thus, the **first quarter of the year marked diverse development of the major indicators characterizing the condition of the capital market in Bulgaria** (interpreted and measured traditionally through the indicators of Bulgarian Stock Exchange – Sofia AD). Excluding compensatory instruments, but including block transactions the stock exchange turnover and volume of trade remained at lower levels compared to the previous quarter. However, the market capitalization and SOFIX index exceeded the 2002 end values.

The capital market in Bulgaria remains underdeveloped. Low liquidity continues to be one of the basic problems. Despite the large number of issues registered for trading liquid positions are only a few and changing. The latter is partially confirmed by the change in the SOFIX index made by the stock exchange in March. Despite the increased number of issues included in the calculation of the index, one of the largest Bulgarian companies in the past was to be excluded. This company (Chimko AD, Vratza) used to be among the most attractive companies for trading but it ceased to meet the criteria for inclusion in the stock exchange index. Creditors filed a claim against it requesting opening of a bankruptcy procedure.

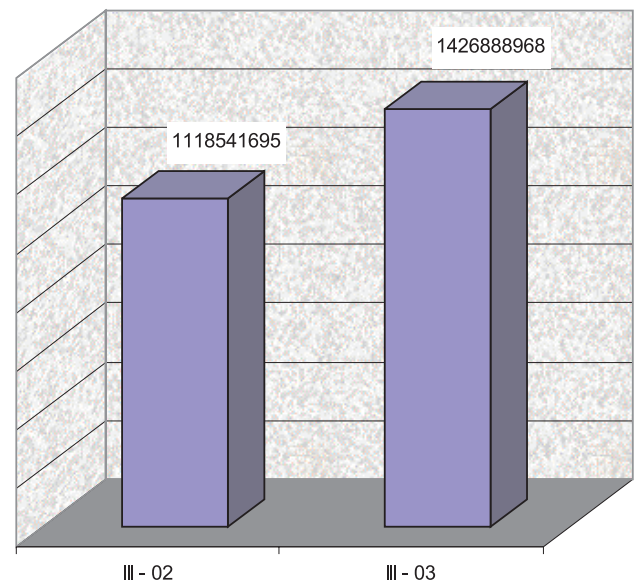
Comparisons to the respective period of 2002 also result in contradictory conclusions. As regards the turnover and traded volumes on the Bulgarian Stock Exchange – Sofia AD in the first quarter of 2003 a decline is observed versus the same period of last year (Figure 15). At the same time capitalization goes up (Figure 16). Overall, the decrease or holding up of traded volumes and turnover continues to express the **trends of consolidation of ownership and concentration of trading onto a smaller number of issues at the expense of low or even degrading liquidity of most of the quoted securities. At the same time most of the securities included in SOFIX (as well as some others) have good liquidity already accepted well by investors and providing good basis for further promotion and development of the market.**

Figure 15. Trading on the Bulgarian Stock Exchange – Sofia AD (first quarters of 2002 and 2003)



Source: according to data from the Bulgarian Stock Exchange – Sofia AD, monthly bulletins

Figure 16. Market capitalization of the Bulgarian Stock Exchange – Sofia AD markets at the end of the period (BGN)



Source: according to data from the Bulgarian Stock Exchange – Sofia AD, monthly bulletins

During the period the financial statements of public companies were to be published for the last quarter of 2002 due in accordance with the last amendments to the law. Like in previous reporting periods, many of the companies did not file again their statements in time which confirms the problem with the further need for improvement of accounting and regulatory practices and principles of corporate management.

This again underlies the conclusion that the dependence of prices of traded companies on public disclosure of corporate events remains contradictory on the Bulgarian market.

There was some **movement on the bonds market** on the Bulgarian Stock Exchange – Sofia AD during the first quarter of the year. Registered for secondary trading on the stock exchange floor were the bond issues of Overgas Inc AD and AutoBohemia AD (privately placed before and fully subscribed). In January a bond issue of Dupnitsa municipality was registered on the primary market of the stock exchange. Nevertheless, only five deals in bonds were concluded on the primary market during the quarter. Only 43 corporate bonds transactions are concluded during the quarter on the official markets of Bulgarian Stock Exchange – Sofia AD the total turnover being BGN 14 m (most of which are registered secondary deals in Overgas Inc bonds). On the non-official markets of the stock exchange over the quarter the total number of corporate bonds transactions is 18 with a total turnover of a little over BGN 1 m.

In the first quarter of the year **auctions for sales of rights** were held for the second time (unused rights to new issues of three companies – Bentonit AD, Lead and Zinc Complex AD and Toplivo AD). In spite of the insignificant volumes, this new practice is so far successful and it confirms the potential of the trading mechanism of Bulgarian Stock Exchange – Sofia AD. Sviloza AD was the first public company which increased its capital in 2002 via an issue of tradable rights. The obligatory condition for the issue of rights with capital increase was introduced with the amendments to the Act on Initial Public Offering of Securities in the summer of 2002, the idea being to better protect the interests of small investors.

Trading in Compensatory Instruments

The start of the trading in compensatory instruments on the floor of the Bulgarian Stock Exchange – Sofia AD was among the leading events in the area of the capital market in 2002.

Generally, the positive expectations are justified so far, as seen also in the first quarter of 2003.

At the end of August the Board of Directors of the Bulgarian Stock Exchange – Sofia AD made a decision for the registration of compensatory instruments (on the Non-official market, Compensatory Instruments market segment). Trading started in the three issues of securities comprising the group of compensatory instruments under the Act on Compensatory Instruments Transactions – these compensatory warrants under the Act on Compensation of Owners of Nationalized Property, housing compensatory warrants under the Act on Compensation of Owners of Nationalized Property, and registered compensatory bonds under the Act on Ownership and Use of Farm Land and the Act on Restitution of Ownership over Forests and Land from the Forestry Stock. The Act on Compensatory Instruments Transactions adopted earlier in the year put an end to the issuing, deals and payments under the previous procedure with the securities in question. On 2 September, 2002 trading in compensatory instruments started again but now solely on the floor of the Bulgarian Stock Exchange – Sofia AD.

Statistics for the period January – March 2003 show the following: a total of 4 121 transactions in compensatory instruments are carried out with a turnover of BGN 17 534 456 which presents a significant decline compared to the previous quarter. In addition, however, block transactions in compensatory instruments are registered on the stock exchange – these are 19 deals in compensatory warrants with a total turnover of BGN 7 761 893 (an increase versus the previous quarter) and 20 transactions in registered compensatory bonds with a total turnover of BGN 22 269 527 (which is a higher turnover but with a lower number of transactions compared to the previous quarter). Compensatory instruments were traded over the quarter at prices of 20 to 25 per cent of the nominal value which was in the range of the previous quarter but with a narrower margin.

The COBOS system

At the end of February the Board of Directors of the Bulgarian Stock Exchange – Sofia AD approved finally the rules for registration and operation with the system for electronic submission of orders via Internet by customers of members of the stock exchange and fixed 4 March as the date of coming into effect of these rules. Thus, the beginning of March marked the official start of the so-called COBOS system (client order-book online system). The introduction of this system is aimed at both facilitating Bulgarian investment intermediaries and providing opportunity for individual and institutional investors from the country and abroad (through direct access to the trading system of the exchange) to file easily their orders for purchase or sale of securities.

COBOS is an Internet-based application for authorized and protected real-time access to the trading system of the exchange providing a possibility for filing of orders for transactions by customers of stock exchange members. Subscribers to COBOS can be only members of the stock exchange and participants on a non-official market who carry out transactions in the trading system via a remote access. Users of COBOS can only be stock exchange brokers and system administrators, as well as customers of the subscribers. Subscribers receive personal certificates with broker's or administrator's rights upon payment of the fees due. Fees (VAT exc.) are BGN 1000 for a subscriber and BGN 60 for a customer. Customers of subscribers receive certificates with customer's rights upon signing a contract with the customer.

Introduction of COBOS is viewed upon as an important step towards promoting and facilitating access and, in the end, enhancing exchange trade liquidity.

Legal and regulatory environment

As regards the **legal and regulatory environment** the most important event in the first quarter of 2003 was the constitution of the new unified supervisory body – **the Financial Supervision Commission** – as a result of the **Act on the Financial Supervision**

Commission passed at the end of last year. The act stipulates mainly the unification of supervision over the non-banking financial sector in Bulgaria – capital market, insurance and social security of the fully funded type. Cutting costs, shrinking of existing administration and enhancing efficiency were among the main motives underlying the idea of integrated supervision. By a Presidential decree the newly adopted law was returned for review. The President's veto repeated in its motives the most common arguments of the opponents to the draft law in 2002. The President contested the proposal that decisions of the Financial Supervision Commission can not be appealed before the court, as well as some of the provisions related to the annual fees to be paid by the entities – subject to supervision by the future sole financial regulator. However, the draft law was passed again by the Parliament in January of this year without modifications and was attacked by a part of the opposition before the Constitutional Court. In April the Constitutional Court admitted this constitutional case to hearing.

In the mid of March the Parliament elected the members of the Financial Supervision Commission and it started functioning. The Department of Supervision over Investment Activities in the new commission practically assumed the functions and the structure of the State Securities Commission operating so far.

By the end of the first quarter of 2003 the **Act on Companies with Special Investment Purpose** was not still adopted at second reading, though this happened a bit later.

The condition of banks in Bulgaria continues to be stable with excellent indicators of capital adequacy and liquidity and parallel to this, a well functioning banking supervision. At the end of the first quarter there are 34 banks in Bulgaria, out of which 27 are banks licensed to operate in the country and abroad, there is one bank licensed to conduct transactions only within the country and there are six branches of foreign banks.

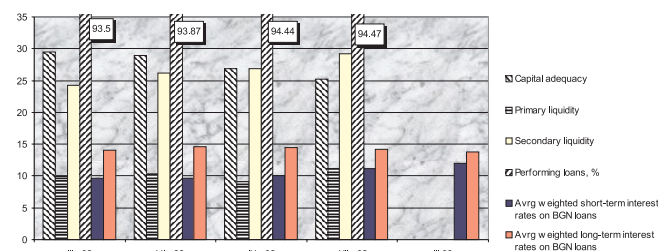
Statistics of the banking system

According to BNB data as of the end of March 2003 the banking system has assets at the value of BGN 14 976 602 thousand, while at the end of 2002 these amounted to BGN 14 557 124 thousand (this presents an increase of BGN 419 478 thousand in the first quarter of 2003). At the end of March deposits amounted to a total of BGN 11 158 984 thousand, while at the end of 2002 these amounted to BGN 11 282 160 thousand (which is a decrease of BGN 123 176 thousand for the first quarter). In March the current profit of the banking system was BGN 125 420 thousand while in the last month of 2002 it was BGN 266 625 thousand. According to the last available data from BNB the total capital adequacy of commercial banks at the end of December 2002 was 25.22 per cent (without group five), while this ratio was 26.84 per cent at the end of September (and 31.32 per cent at the end of 2001). At the end of December 2002, total primary liquidity of the banking system was 11.2 per cent, and secondary liquidity was 29.25 per cent (the respective figures for the end of September were 9.03 and 26.88 per cent, and for the end of 2001 - 13.47 and 25.47 per cent, respectively). Some of these indicators are illustrated in Figure 17.

Thus, the banking system as a whole continued over the last quarter to increase its assets but experienced a decline in the levels of deposits and current profit. However, the current profit of the banking system at the end of the quarter exceeded the one of March 2002. The ratio between net interest income/other non-interest income is increased (from 2.30 and 2.25 at the end of 2001 and 2002, respectively, since

at the end of 2000 it was 2.18, this ratio reached 2.54 at the end of March 2003) which suggests underdevelopment and insufficient diversification in the banking business. The capital adequacy ratio at the end of 2002 is lower than the one at the end of 2001, and yet it is relatively high and presents evidence of the stability of the system. The liquidity ratios of the banking system for December 2002 are higher than those three months earlier. All this can again be interpreted as a sign that there exists **stability in the banking system of Bulgaria but its efficiency and degree of development remain questionable.**

Figure 17. Selected indicators of the banking system (%)



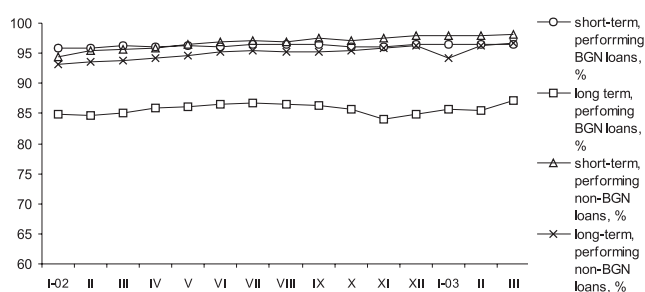
Source: according to BNB data, monthly information bulletins

Lending to the non-government sector shows a clear trend of increase (under the Currency Board arrangements these are namely the loans from commercial banks that include loans to non-financial state-owned enterprises, private enterprises, households and non-banking financial enterprises). From BGN 4 374 627 thousand at the end of 2001, receivables on loans to the non-government sector reached BGN 6 250 741 thousand at the end of December 2002. At the end of March 2003 receivables on loans to the non-government sector became already BGN 6 662 728 thousand.

Newly contracted loans from commercial banks for the first three months of 2002 were at a total value of BGN 991.4 m, while for the first three months of 2003 newly contracted loans amounted to a total of BGN 1 235.34 m (a growth of almost 25 per cent). The condition of the loan portfolio is also improving - if 93.87 per cent of all categories of loans in the banking system were classified as performing at the end of June 2002, at the end of September

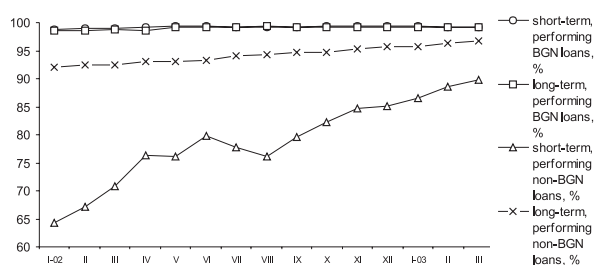
this figure is 94.44 per cent, and at the end of 2002 - 94.47 per cent performing loans (Figure 17). This general conclusion holds true in particular with regard to receivables on loans to private businesses and households - there the percentage of performing loans increases or is maintained again high in the first three months of 2003 (Figures 18 and 19).

Figure 18. Condition of the loan portfolio: private businesses (revised data after December 2002)



Source: according to BNB data, monetary report and own calculations

Figure 19. Condition of the loan portfolio: households (revised data after December 2002)



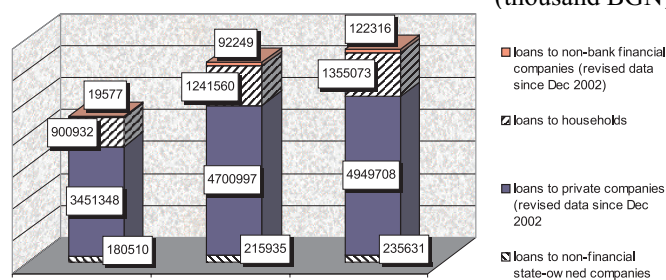
Source: according to BNB data, monetary report and own calculations

Interest rates on short-term loans in BGN in March 2003 are higher compared to the end of 2002, while with long-term loans in BGN these are lower (Figure 17 again). The dynamics of loans reveals some other interesting short-term trends (by currency, term and borrowers). Thus, for example, the review of receivables on loans to the non-government sector illustrates highest growth of the credit exposition simultaneously to private enterprises and to households, but their relative share remains practically unchanged (Figure 20).

Figures 21, 22 and 23 present the dynamics of newly contracted loans for 2001 and 2002. The first three months of 2003 indicate increased lending activity compared to the same period of 2002. As

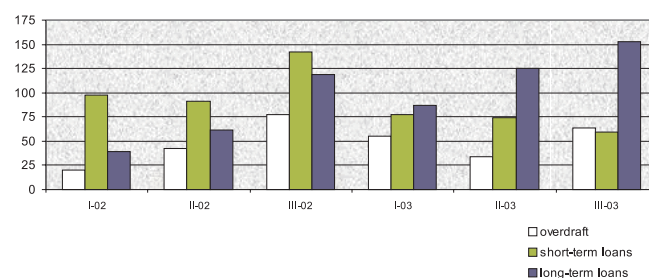
regards the terms and currencies, however, there is an interesting trend of increase of the share of long-term versus short-term loans in BGN and Euro, while with loans in USD the increase is relatively higher with short-term loans. This reflects not so much interest rate dynamics, but rather the growing investment activity in the country, taking into account the foreign exchange risk (under the arrangements of a Currency Board and the Euro as a reserve currency for Bulgaria) and the expectations for ongoing decline of the USD exchange rate in the short-term.

Figure 20. Receivables on loans to the non-government sector (thousand BGN)



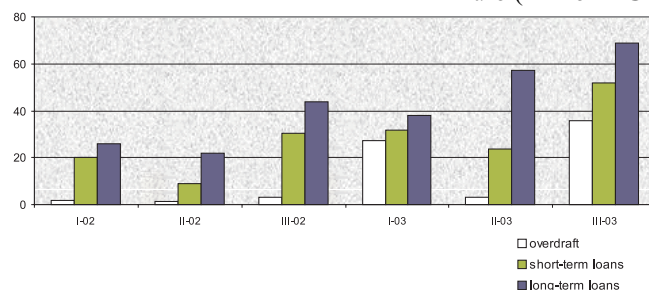
Source: according to BNB data, monthly information bulletins

Figure 21. Newly contracted loans from commercial banks in BGN (million BGN)



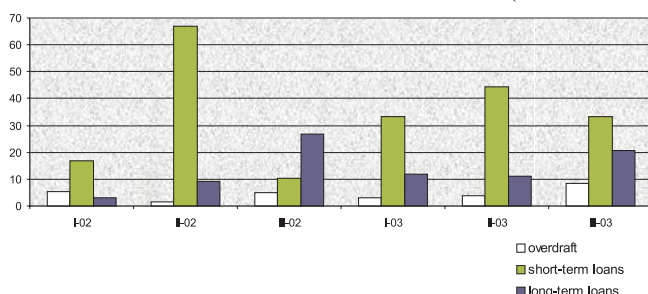
Source: according to BNB data, monthly information bulletins

Figure 22. Newly contracted loans from commercial banks in Euro (million BGN)



Source: according to BNB data, monthly information bulletins

Figure 23. Newly contracted loans from commercial banks in USD (million BGN)



Source: according to BNB data, monthly information bulletins

Restructuring and privatization in the sector

Via various channels like privatization, opening of representation offices, branches and newly established banks, **foreign interest in the banking system of Bulgaria is already prevailing both in the control over equity and managed assets.**

According to the last quoted data by BNB²⁰, 83.4 per cent of the total assets of the banking system are owned by private persons at the end of 2002. At the same time foreign banks and investors control 72 per cent of bank assets.

During the last months of 2002 and the beginning of 2003 significant developments were observed with regard to the privatization of the last two large state-owned banks, and again foreign investors and consultants had the leading role. In the mid of 2002 the contract was signed for the sale of **Biochim AD commercial bank** to Bank Austria - 99.59 per cent of Biochim's capital were sold for EUR 82.5 m. The banking group Bank Austria Kreditanstalt was present in Bulgaria until that time through its subsidiary HVB Bulgaria. The scheme of the buyers provided for the subsidiary bank to merge into Biochim. The privatization of Biochim and the merger with HVB Bulgaria were completed by the end of 2002 - Biochim was transformed by acquiring HVB Bulgaria and the latter, as a result of the merger, was terminated without liquidation. Then the capital of Biochim was increased and the whole new issue was subscribed by Bank Austria. Following this transaction the share

of Bank Austria in Biochim grew to 99.68 per cent.

The last large state-owned bank remains **DSK Bank AD** which together with Encouragement Bank accounts for the remaining 14.2 per cent of the state-owned share in the banking assets (the municipal share is 2.4 per cent). As early as July 2002 five potential candidates were selected as consultants for the privatization of DSK Bank. Later on, based on additional presentations, J.P. Morgan was chosen as the final consultant. In October 2002 the state interest of 75 per cent in DSK Bank was transferred to the Bank Consolidation Company and thus the sale of the bank could now be finalized. The bank privatization procedure started officially on 9 December 2002 by the publication of an invitation to potential investors in Financial Times and in a Bulgarian daily.

As of the mid of December 2002 five potential buyers were known to have expressed their interest to DSK Bank. The end of January 2003 was the deadline for filing of indicative offers by candidate-buyers. Within the time limit offers were submitted by the Austrian Erstebank, the Hungarian OTP and the Greek Pyreus bank. Up to 100 per cent of the capital of DSK Bank, but not less than 80 per cent, were offered for privatization. Since all the three potential buyers promised to pay a better price per share if offered 100 per cent of DSK Bank, BCC decided to announce for sale the whole block of shares. BCC admitted all the three candidate-buyers to the due diligence of DSK Bank.

By the end of March it was officially announced that final offers for the purchase of DSK Bank would be accepted by 10 April. However, only two of the buyers filed their offers within the time limit, the Austrian Erstebank and the Hungarian OTP. Later OTP was chosen as the buyer of DSK Bank at the price of EUR 311 m.

Development of the Regulatory Framework

No amendments, directly related to the banking sector, were made to the regulatory framework in the first quarter of 2003. **The draft law for amendments**

²⁰ Source: BNB Annual Report 2002

to the **Banking Act** submitted to the Parliament in December 2002 by a group of MPs of the ruling coalition is still not passed even at the stage of first reading. The only proposal in this draft was to introduce a requirement that at least one Bulgarian citizen be elected in the managing bodies of a bank who speaks Bulgarian and who has lived in Bulgaria for at least a year before their appointment. The draft was justified with the need for better communication between commercial banks and official Bulgarian institutions, easier adaptation to the Bulgarian market and better knowledge of the situation in the country. Underlying this justification were the fears of some representatives of the banking circles in our country that Bulgarian bankers' access to the top management levels of the banks would be limited since most of them are under foreign control.

Social Security

In the first quarter of 2003 major focus points in the social security sphere were given upon the first financial results of the introduced minimum social security thresholds per branches and professions and of the mandatory registration of labor contracts at the NSSI announced by MLSP and NSSI, the achieved 2002 return of invested pension fund resources, the authorization by the Commission on Protection of Competition of the merger of Bulgarsko Pensionno-osiguritelno Druzhestvo AD (Bulgarian Pension Insurance Company) into Doverie Pension Insurance Company (PIC) and the passed Act on the Financial Supervision Commission which is the new supervisory authority on the social insurance market. The National Assembly's social commission continues the paragraph-by-paragraph discussion of the new Social Security Code for second reading.

The first financial results of the introduced minimum social security thresholds per branches and professions and of the mandatory registration of labor contracts at the NSSI since the beginning of 2003, announced by the National Social Security Institute, reveal that **the fear of mass reappointment of workers and employees on lower paid positions and professions with lower social security thresholds and wages did not come true. According to NSSI's data, by 27 March payments to social security funds increased generally by BGN 92.7 m as compared to the same period of 2002; 38 000 registered unemployed proved employed under labor contracts and around 250 000 people emerged from the shadow economy.** Around 320 000 of the total of 1 321 375 labor contracts registered with the NSSI as of 27 March 2003 are new, which means that they might be for people who have recently worked in the gray sector. In the first two months of 2003 estimated social security income of people employed under labor or service contracts registered an increase of nearly 10 per cent compared to 2002. The basic wage declared in the established labor contracts is by 4 per cent higher compared to the figure registered

by NSI for October 2002. Higher collection of social security contributions to State Social Security funds is a good indication for possible future lowering of the social security burden for employers and employed individuals and for possible raising of pensions level. Results for the 2002 return distributed on an annual basis under individual lots of persons insured in supplementary pension insurance funds, announced by the Social Security Supervision Department at the new Financial Supervision Commission, reveal that saving in a private pension fund is an excellent investment. Voluntary pension fund return varies from 7.03 per cent in Saglasie AD PIC (the lowest return) to 11.55 per cent in Lukoil-Garant Bulgaria AD PIC (the highest return). Realized return is higher than the inflation rate reported at 3.80 per cent. Excess over the average annual basic interest rate reported at 3.96 per cent and over the average interest rate on one-year fixed bank deposits reported at 5.34 per cent is registered. Occupational pension fund return varies within the range of 9.42 per cent in Bulgarsko Pensionno-osiguritelno Druzhestvo AD to 12.09 per cent in Lukoil-Garant Bulgaria PIC. Minimum return is fixed at 6.47 per cent and results reveal that all occupational pension funds are above the fixed minimum. Realized return on individual lots of persons insured in these funds is higher compared to the inflation rate as well as to the average annual basic interest rate and the average interest rate on one-year fixed bank deposits for 2002. 2002 realized return in the universal pension fund varies from 9.38 per cent in Allianz Bulgaria PIC to 17.95 per cent in Lukoil-Garant Bulgaria PIC. It is also higher compared to the inflation rate, the average annual basic interest rate and the average interest rate on one-year fixed deposits. Investment in voluntary pension is comparable in terms of risk to bank deposits and the continuing strict control over pension companies exercised by the Social Security Supervision Department at the new Financial Supervision Commission guarantees security in the management of funds for social security purposes accumulated under individual lots. Under the current legislation pension companies are obliged to invest minimum 50 per cent of their assets in government securities and/or bank deposits, which have the

lowest risk margin. The new Social Security Code provides for certain liberalization of the investment regime for voluntary pension funds. Lower percentage of mandatory investments in government securities is expected for these funds, but the strict control and supervision of their activity will continue, and pension companies are in principle conservative institutional investors, which do not take great risk in managing the funds of the insured.

The objective of the merger of Bulgarsko Pensionno-osiguritelno Druzhestvo AD into Doverie AD PIC, which was authorized by the Commission for Protection of Competition, is to improve the operational efficiency of a pension insurance company with a view to higher final financial result and opportunity to lower the service price for the insured, on one hand, and to guarantee higher stability by increasing the number of the insured in a pension fund, on the other hand. **Doverie PIC estimates the new market share of the pension company at around 42-43 per cent, which will not constitute substantial increase of the market share of Doverie PIC and, therefore, there is not any threat of monopolistic position on the social insurance market.** This is the first step towards consolidation of the Bulgarian pension market, with seven pension companies expected to operate now on the social insurance market in Bulgaria – Doverie, Saglasie, Allianz Bulgaria, Rodina, Newton-Sila, I N G, and Lukoil-Garant Bulgaria. The process of consolidation of Bulgaria's social insurance market is expected to continue in the future, with pension companies becoming a major actor on the capital market in the country.

The Act on the Financial Supervision Commission was passed at the end of January 2003 and took effect as of 1 March 2003. Thereby an opportunity for synchronized regulation and supervision of the whole non-bank financial sector in Bulgaria was created. The single supervisory authority of the social insurance, insurance and capital markets is expected to guarantee more efficient control, better protection of the consumers of all non-bank financial services and more efficient utilization of human and material

resources, which is an important precondition for the integration of Bulgaria's non-bank financial sector in the European economic area.

The new Social Security Code did not reach second reading in Parliament in the first quarter of 2003, either. The draft is currently discussed paragraph by paragraph for second reading in the National Assembly's social commission. **Deputies have agreed so far to eliminate the requirement for the minimum number of persons insured in occupational and universal pension funds**, thereby solving the problem of the occupational funds of Rodina Lukoil-Garant, I N G, and Newton-Sila, which for two years following their licensing did not manage to accumulate the required number of 15 000 insured persons to continue their operation. Experts are of the opinion that the transfer of insured persons from one supplementary pension fund to another would affect the image of the funds and would create opportunities for unregulated pressure by social insurance agents for transfer of insured persons with a view to achieve the obligatory limit for the corresponding funds, or for keeping the insured persons in the funds which have already achieved the required number of members. Finally, supplementary pension insurance companies agreed to the elimination of these limits under the condition that the issue would be discussed in the transfer regime context. Discussion and approval of legal texts regulating the terms and procedure of transfer of insured persons to one fund or another is pending.

Deputies also voted a text according to which a **pension insurance company may take a loan up to 10 per cent of its equity capital**, if the loan is utilized for acquisition of fixed tangible assets (FTA), which are indispensable for company's operation, and is taken for a period of not more than 3 months. Authorization by the supervisory authority was formerly required.

With respect to the capital of the pension company, **an increase of the minimum amount of capital from BGN 3 m to BGN 5 m** was voted with a view to create higher security for the insured.

The social commission also voted a text according to which **NSSI's claims of unpaid State Social Security contributions and of improperly incurred social security expenditures will be collected with penal interest equal to BNB's basic interest rate plus 20 percentage points.** Given the large amount of liabilities to NSSI (around BGN 400 m), criminalization of the failure to pay social security contributions is expected. The texts have been worked out and are expected to be introduced along with the other amendments to the Penal Code.

A ceiling of voluntary social insurance contributions has been introduced since the beginning of 2003 as **physical persons may deduct up to 10 per cent of their income prior to taxation, if they make payments for a third pension, voluntary health insurance** and unemployment insurance. Such a ceiling did not exist until now. According to the president of the Bulgarian Association of Supplementary Pension Insurance Companies, the full tax preference for voluntary social insurance contributions should have been preserved for not less than another five years with a view to convince the insured in the positive aspects of the pension reform and in the stability of the legislation in this area. The preference of 100 per cent input exemption of contributions is a good incentive for the development of voluntary social insurance. Amendments to the Personal Income Taxation Act settled the issue of the 20 per cent taxation of amounts upon transfer of individual lots to a third person. The tax shall be payable by the transferor of the funds and the new right holder shall not pay any tax upon receipt of pension. A single tax of 20 per cent shall be payable in the event of pre-term drawing of funds from the individual lots of insured persons.

The authorization of the pension company - custodian bank relatedness was undoubtedly the most widely discussed case in connection with the new Social Security Code. Unlike former social security legislation, the new Social Security Code provides that pension insurance companies will not be allowed to sign more than one custodial service contract for each supplementary pension insurance

fund they manage. Along with the functions of keeping the assets of pension companies, the custodian bank also has business and control functions. The fact that any pension company could increase the circulation of the funds for social security purposes in the custodian bank prior to their investment, if the two entities have common interests, or decrease it in the event of different interests, constitutes conflict of interests, and the question of whether that is to the benefit of the insured is widely discussed. Experts also detect conflict of interests in the legal opportunity to make deposits in the custodian bank up to 10 per cent of funds' assets, because there is no legal ban on the negotiation of higher interest rates on the deposits made by the corresponding pension fund in the custodian bank, which is a related person to the pension company. The question is about the so-called artificial higher return, which can be adjusted at a later stage. There is also a possible conflict of interests in terms of the control functions performed by the custodian bank. If the custodian bank and the pension company are one person, nothing could make them notify the supervisory authority upon investment of the funds for social security purposes in an illegal financial instrument. The belief that the authorized custodian bank-pension company relatedness creates better conditions to guarantee the security of insured persons gained ground in the long run.

The texts of the new Social Security Code approved by the Commission on Labor and Social Policy permit pension insurance company-custodian bank relatedness, and prohibit pension insurance company-investment broker relatedness and custodian bank-investment broker relatedness.

According to pension insurance company representatives and independent experts, these texts, which remain to be voted at second reading in the plenary room, could do much harm to the development of the pension system in Bulgaria. The new Social Security Code is undoubtedly a step towards improvement of Bulgaria's social legislation, but controversial points do exist yet.

On 6 February 2003 Bulgaria's and Macedonia's ministers of labor and social policy signed in Sofia a Social Security Agreement between the Republic of Bulgaria and the Republic of Macedonia, as well as an Administrative Arrangement on its implementation. The agreement covers nearly all social security risks under Convention N102 of the International Labor Organization, in observation of the principle of equal treatment of nationals, equality of territories, retention of acquired rights, accumulation of social security periods respected under the legislation of the two countries, and of the principle of proportionality of payments in calculating pension amounts. The signing of Social Security Agreements, which in principle accompany Labor Force Exchange Agreements, is an effective policy to improve labor force mobility and a successful measure to alleviate concerns of current EU Member States about possible pressure on their labor markets after the EU accession of Central and Eastern European countries.

Supplementary Pension Insurance

According to data from the Social Security Supervision Department at the Financial Supervision Commission, as of 31 March 2003 the total number of the insured in supplementary pension funds was 1 894 678 people. The insured individuals in voluntary pension funds were 486 812, in universal pension funds – 1 250 325 and in occupational pension funds – 157 541. As of 31 March 2003 total net assets of supplementary pension insurance funds amounted to BGN 360 416 thousand. Voluntary pension funds account for 56 per cent of the assets, occupational pension funds - for 29 per cent, and universal pension funds - for 15 per cent. As of end of November 2002 assets of pension funds amounted to BGN 310 341 thousand, which means that for four months assets of pension funds have registered a growth of 16 per cent. As of 31 March 2003 the tendency to invest assets of pension funds mainly in state-issued or state-guaranteed securities and in bank deposits in the country persists, with only Lukoil-Garant Bulgaria AD making steps to invest in foreign securities.

Universal Pension Funds

According to data from the Social Security Supervision Department at the Financial Supervision Commission, as of 31 March 2003 the total number of the insured in universal pension funds was 1 250 325 people. Dovereie AD PIC attracted the highest number of insured persons (489 019 people, or 39 per cent), followed by Allianz Bulgaria AD PIC (253 287 people, or 20 per cent), and Saglasie AD PIC (160 375 people, or 13 per cent). As of 31 March 2003 assets accumulated in universal pension funds amounted to BGN 54 370 thousand. Dovereie AD PIC accumulated the highest amount of assets (BGN 19 936 thousand, or 37 per cent), followed by Allianz Bulgaria AD PIC (BGN 12 180 thousand, or 22 per cent) and Saglasie AD PIC (BGN 6 765 thousand, or 12 per cent). As of 31 March 2003, universal pension funds made 77.81 per cents of their investments in state-issued or state-guaranteed securities, 16.48 per cent - in bank deposits in the country, 4.98 per cent - in securities accepted for trading on the regulated securities market, 0.45 per cent - in real estate, 0.26 per cent - in municipal bonds, and 0.02 per cent - in foreign securities. The universal pension fund Lukoil-Garant Bulgaria is the only fund which made investments in foreign securities accepted for trading on the regulated securities markets.

Occupational Pension Funds

According to data from the Social Security Supervision Department at the Financial Supervision Commission, as of 31 March 2003 the total number of the insured in occupational pension funds was 157 541 people. Dovereie AD PIC attracted the highest number of insured persons (55 936 people, or 36 per cent), followed by Allianz Bulgaria AD PIC (35 010 people, or 22 per cent) and Saglasie AD PIC (29 941 people, or 19 per cent). As of 31 March 2003 net assets accumulated in occupational pension funds amounted to BGN 103 684 thousand. Dovereie AD PIC accumulated the highest amount of assets (BGN 38 515 thousand, or 37 per cent), followed by Allianz Bulgaria AD PIC (BGN 26 924 thousand, or 26 per cent) and Saglasie AD PIC (BGN 18 770

thousand, or 18 per cent). As of 31 March 2003, occupational pension funds made 72.68 per cent of their investments in state-issued or state-guaranteed securities, 18.72 per cent - in bank deposits in the country, 6.95 per cent - in securities accepted for trading on the regulated securities markets, 0.87 per cent - in real estate, 0.76 per cent - in municipal bonds, and 0.03 per cent - in foreign securities accepted for trading on the regulated securities market. The occupational pension fund Lukoil-Garant Bulgaria is the only fund which made investments in foreign securities accepted for trading on the regulated securities markets.

Voluntary Pension Funds

According to data from the Social Security Supervision Department at the Financial Supervision Commission, as of 31 March 2003 the total number of the insured in voluntary pension funds was 486 812 people. Allianz Bulgaria AD PIC attracted the highest number of insured persons (250 733 people, or 52 per cent), followed by Doverie AD PIC (90 067 people, or 19 per cent) and BPOD AD (32 878 people, or 8 per cent). As of 31 March 2003 net assets accumulated in voluntary pension funds amounted to BGN 202 362 thousand. Allianz Bulgaria AD accumulated the highest amount of assets (BGN 109 349 thousand, or 54 per cent), followed by Doverie AD PIC (BGN 31 062 thousand, or 15 per cent) and Lukoil-Garant Bulgaria AD PIC (BGN 16 470 thousand, or 8 per cent). As of 31 March 2003 voluntary pension funds made 58.52 per cent of their investments in state-issued or state-guaranteed securities, 34.90 per cent - in bank deposits and mortgage bonds, 3.92 per cent - in real estate, 1.44 per cent - in securities accepted for trading on the regulated securities market, 0.64 per cent are under Other Investments, 0.55 per cent - in municipal bonds, and 0.04 per cent - in foreign securities. The supplementary voluntary pension fund Lukoil-Garant Bulgaria is the only fund which made investments in foreign securities.

Employment, Unemployment and Labor Market Policy

After the sizable decrease of the number of unemployed in 2002 of 12.4 per cent, the downward trend in the number of unemployed registered at the labor offices was preserved in the first quarter of 2003. In January the unemployment level was 17.46 per cent according to this indicator, dropping down to 15.69 per cent in March.

NSI's labor force surveys register **parallel increase of employment** owing to new job opportunities both under MLSP's programs and in the economy as a whole. MLSP projects not less than 100 000 jobs under subsidized employment programs.

Implementation of the active labor market policy and its specific measures, which were largely launched in 2002 as pilot projects, will continue in 2003. All preconditions for successful implementation of the multitude of programs and initiatives in this area, taking into account pilot phase results, are in place.

Latest amendments to the Employment Promotion Act took effect since March 2003. Incentives for employers, who hire unemployed, basically from risk groups (like single parents and people at pre-retirement age), are thereby introduced. The objective of these measures is to revive the labor market and promote job opportunities.

The National Program "From Social Assistance Towards Employment" enters its most significant phase with 600 approved projects. These will provide jobs to 35 000 people, with the program gradually covering 100 000 people. At this stage, the greatest challenge is how to provide employment with parallel achievement of the more important goal - to improve the employability of a large group of people. The challenge is to find a way to reintegrate in the society these uneducated, unqualified or permanently unemployed people by engaging them in adequate forms of employment. Their inclusion in literacy and training courses is pending. The institutions in charge of program implementation are faced with the very important task to develop training programs and find adequate forms and mechanisms to motivate the

participants. There is also progress, within the program again, in the building of institutional capacity through the set up of special units to support employment programs implementation and of international project units at the regional employment services.

A new employment and social assistance project was launched in four Bulgarian municipalities: Blagoevgrad, Botevgrad, Pravetz, and Etropole, in the first quarter of 2003. The Social Services In Return For New Jobs Project is initiated by MLSP and UNDP in partnership with municipalities and local employment and social assistance services. Such projects are a promising example of an integrated approach to social problems and of the cooperation of government institutions, donor organizations and local authorities.

The most important event in the first quarter of 2003 was the agreement, which Bulgaria signed with the World Bank for a loan of EUR 50.8 m for implementation of a Social Investments and Employment Promotion Project. The objective of the project is to contribute for improvement of the living standards of people in the so-called poverty niches concentrated in different Bulgarian regions, of permanent unemployed and of ethnic minorities. These extremely vulnerable social groups are exposed to social isolation, insufficient social capital, limited access to markets and basic services, low education and employment level. Consequently there is a need of a complex approach to overcome these unfavorable conditions and find ways to take these people out of the vicious circle of poverty and its recurrence generation after generation.

The loan will be utilized in accordance with the priorities in the new social policy strategy - differentiated approach to different social groups, active social policy, decentralization and improvement of the quality of social services. The project will be implemented by the Social Investment Fund under the guidance of MLSP. It will contribute, in cooperation with municipalities and local communities, to more than 700 000 man-days of employment generated by small local infrastructure

projects and active interventions on the labor market. The project will also provide job opportunities for workers laid off in restructured sectors, who need short-term employment in the period of transition to some other job.

All these labor market measures and projects are a good basis to decrease unemployment and increase employment in Bulgaria in a short-term perspective. But they should also pursue long-term objectives so that the qualitative and quantitative parameters of employment in Bulgaria guarantee fulfillment of EU's economic and social criteria. This is true in the first place for the qualification level of Bulgaria's labor force and its adaptability to a dynamically changing economic environment.

Income and Living Standards

The nominal and real increase of the incomes of Bulgarians, registered by NSI on the basis of data for wages and household budgets, continued in the first quarter of 2003. Compared to the same period of the previous year, the wage of total employed registered an increase of 5.5 per cent, and total monthly income average per household registered an increase of 8.9 per cent. These data suggest an emerging permanent upward trend in the incomes of Bulgarians, with first signs noticed in the second half of 2002. Major factors, which contribute to this positive effect, include: continuing low inflation level, unemployment decrease programs and differentiated higher amounts of some social payments, positive economic dynamics.

Income statistics data reveal similar trends to those registered by NSI's regular consumer survey conducted in January 2003. The consumer trust indicator registered an increase of 2.8 percentage points in the period October 2002 - January 2003. Opinions of consumers about the changes in the financial situation of households in the last 12 months, as well as their expectations for the next 12 months are more optimistic. The favorable trend registered by the latest surveys of inflation assessments for the previous 12 months is preserved. But expectations

about consumer price changes in the next 12 months are more pessimistic compared to opinions expressed three months earlier. In January 2003 consumers are more optimistic in their expectations about unemployment. Overall, survey results indicate a rather stable and optimistic situation in the economy and in the living standard of Bulgarians, which however does not indicate notable improvement of the latter.

Social Assistance

In the first quarter of 2003 social assistance witnessed an important institutional change. **In accordance with latest amendments to the Social Assistance Act, an Agency for Social Assistance was set up to replace the currently operating special body.** The new structure provides better opportunities for social protection of people in need and for implementation of a differentiated approach in this area. The change in the social assistance governance structure is an element of the fundamental change of social policy philosophy. The objective is to improve management by differentiating the functions of the state and the municipalities in the administration, financing and control of social activities.

The Agency for Social Assistance will implement Government's policy in the field of social assistance. Its basic activities will include delivery of social services, allocation of social and child benefits, management of specialized social service institutions, etc.

Agency's territorial units include regional social assistance directorates (current regional social assistance centers), having their seats in regional administrative centers, and the Social Assistance Directorates (current municipal social assistance centers) on the territory of each municipality.

Social Partnership

Bulgaria has long-standing and well operating social partnership mechanisms on national level, however at sector, enterprise or municipal level the relationship between employers

and employed does not always go well. Conflicts related to the pending privatization of big enterprises, significant to national economy, like BTC, Bulgartabac, etc. are most serious. The quarter under review was full of demonstrations of social tension in such situations, which further complicate and delay privatization procedures. Trade unions insist on taking more active part in the negotiation of the social clauses of privatization contracts. Such cases should be approached with utmost caution and reasonableness, paying attention not to deny the right of trade unions to be involved in the decisions on such important social issues in their capacity of representative organizations of workers.

Further to recent forms of social dialogue, a decision to set up an Advisory Council on Economic and Social Policy to the President was taken in March. The aim is to involve in the new structure a wide range of experts, representatives of trade unions and employers, non-government organizations, etc.

The regular advisory meetings of employers' organizations and trade unions are a good example of well-functioning social dialogue. This year social partners intend to prepare and sign two national agreements. One between the trade unions and the employers' organizations; the other between the social partners and the Government. The objective of these agreements is to coordinate the general framework and future actions towards improvement of the social and economic situation in Bulgaria.

The new 2003 National Framework Agreement (NFA) signed between the National Health Insurance Fund (NHIF), the Bulgarian Doctors Union (BDU) and the Union of Dentists in Bulgaria (UDB) in force as of 1 April, was undoubtedly the most debated health insurance topic in the first quarter of 2003. **The voluntary health insurance market expanded by another two funds**, with licensing of other health insurance market participants also expected this year. **The new director of the National Health Insurance Fund (NHIF) was not appointed** without a scandal, either. Changes in the list of free or partially covered by NHIF medicines generated **tension in the pharmaceuticals sector between Bulgarian and foreign pharmaceutical companies**, which compete in getting a higher number of medicinal positions of NHIF's list.

Plenty of discussions and controversial points accompanied the signing of the **2003 National Framework Agreement (NFA) between NHIF, BDU and UDB at the end of March**. According to the Ministry of Health, NFA meets more adequately people's health needs and better regulates the delivery and payment of medical services. What is more, it better protects the interests of children, mothers, and chronically ill people, as it incorporates two health priority programs - maternal and children health care. The new health agreement envisages free access to a pediatrician and an obstetrician.

Forty-five new clinical paths are laid down in the new NFA. A new principle is set forth for laboratory tests – the limitation by way of cards, which generated tension among doctors and patients, is eliminated. The portion of the dental service price payable by NHIF is increased. Funds for practices in unfavorable conditions are increased, and general practitioners will also receive higher pay for small children and old people.

With the gradual build-up of NHIF's information system, general practitioners shall be required to have computers and printers. That will allow some duplicate report forms to be eliminated, others will also be submitted on diskettes with a view to improve

the communication between health service providers and local RHIFs.

In 2003 around 35–40 per cent of hospitals' financial resources are expected to come from clinical paths, with specialized hospitals expected to get more funds from clinical paths, accounting for more than 50 per cent of their financial resources. Around one third of the medical institutions will not manage to fulfill the requirements of NHIF and consequently they will have less financial resources.

The Instruction on the formation of the 2003 wage funds in medical institutions registered as commercial companies with more than 50 per cent state or municipal interest, signed by the Health Minister and constituting a part of the National Framework Agreement, provides for additional pay for medical work under clinical paths.

The envisaged minimum sanction for violations in the NFA amounts to BGN 80, and the maximum is around BGN 2400, with termination of contracts envisaged in the event of recurrent violations.

Contracts with doctors are to be signed by 30 April, and with pharmacies - by the end of May.

The general opinion of the Managing Board of Bulgarian Doctors Union is that the new 2003 National Framework Agreement is a step forward in the health reform because hospital care is actually switched over to real payment for work done and the margin between outpatient care and inpatient care funds is reduced. According to BDU's president, general practitioners fail to understand the philosophy of regulatory standards and illegally boycott the signing of their individual contracts with NHIF. Regulatory standards are expected to get updated every three months on the basis of doctors' individual calculations, and the new health agreement provides for adjustment of the limits for access to specialists and laboratory tests in accordance with people's needs of health services. Besides general practitioners, the Union of Pharmacists is also dissatisfied with the new health agreement signed.

Pharmacists' discontent results from the fact that according to a clause in the 2003 NFA, if a pharmacy does not have some medicine, it is obliged to deliver it to the patient within 8 hours. The Human Medicine Drugs and Pharmacies Act indicates a period of 24 hours.

Within the context of logic the NFA should be better than previous health agreements, but time alone will show whether that is true. The Doctors Union and NHIF should have started real negotiations before the passing of the basic health insurance law and before the approval of NHIF's budget. A higher number of general practitioners are expected to sign contracts with NHIF in 2003 as a result of the eliminated requirement for upper and lower limit of registered health insured persons in the amended Health Insurance Act.

In February the Insurance Supervision Agency, now Insurance Supervision Directorate at the new Financial Supervision Commission, issued two new operational licenses to DZI Health Insurance AD and to Bulstrad - Health Insurance AD. **Higher interest of insurance companies towards the voluntary health insurance market has been recently observed.** According to experts, the reason lies in the underdeveloped market and the good development perspectives. Both the low income of the population and the unfair competition by medical institutions making health insurance on the basis of subscription contracts and by non-licensed commercial companies, which are not controllable by the supervisory authority, are determinative for the extremely narrow voluntary health insurance market. The lack of traditions and information about voluntary health insurance further impedes the development of voluntary health insurance market. Less than 8 per cent of active Bulgarians are currently insured in private health funds, with the percentage expected to increase in the future. 2003 tax changes which introduced a limit of up to 10 per cent on the tax exemption of incomes if spent for voluntary pension insurance, voluntary health insurance and voluntary insurance for unemployment and professional qualification also have negative effect on the

development of voluntary health insurance market.

The doctors lobby defeated that of pharmacists in the appointment of the new health insurance fund director. The new NHIF director is a former member of NHIF's Managing Board and a legal expert in the parliamentary health commission. He signed a management contract instead of a labor contract.

In the first quarter of 2003 the most important point in the **medicinal policy area** was the defined "positive" list of illnesses treatment whereof is payable by NHIF. On 21 March the Bulgarian Association for Protection of Patients filed with the Supreme Administrative Court a complaint with a request to cancel the order of NHIF's director approving the changes in the List of Medicinal Products, Medical Articles and Medicated Foods payable in whole or in part by NHIF, adopted by the Management Board of NHIF. The changes, which took effect on 16 February 2003, limit the reimbursement of 403 out of a total of 1 423 medicinal positions to 25 - 50 per cent. According to complainants, patients' interests are thereby violated and their access to emergency treatment is unjustifiably limited. The truth is that NHIF takes chaotic, hasty and not very thoughtful steps to solve the problem of the inefficient use of funds for medicines.

NHIF was expected to sign with pharmacies contracts for supply of the so-called free or partially payable by the fund medicines for the chronically ill by the end of May. NHIF budgeted BGN 162.7 m for medicines for 2003, whereas in 2002 the fund spent BGN 240 m for this purpose. In 2003 NHIF intends to sign contracts with seventeen Bulgarian producers of medicines and to make a direct payment to them for 27 per cent of the price of medicines. The effect of this direct payment is estimated at nearly BGN 30 m, which otherwise NHIF should pay to pharmacies for mercantile margin to the price of medicines. According to NHIF the early depletion of funds for medicines is a result of the absence of Bulgarian pharmaceutical equivalents of imported medicinal products which are up to three times more expensive.

The problem with the shortage of funds for medicines has not been solved yet. Around BGN 20-22 m are required for medicines per month, BGN 240-250 m per year, with only BGN 162.7 m budgeted for 2003. NHIF's monthly medicines expenditures are almost equal to outpatient care costs. There is no such practice of higher medicines expenditures compared to outpatient care costs anywhere in the world. The problem with the shortage of funds for medicines brought about talks in healthcare circles for opening NHIF's reserve of BGN 780 m which is deposited in BNB and supports the financial stability of the country. The chairman of the parliamentary health commission even proposed an increase of the health insurance contribution from 6 to 8 per cent since 2004 with a view to switch to complete healthcare financing from NHIF. Government measures in the healthcare area are inconsistent, hasty and not very thoughtful. The poor awareness of doctors, who are health system actors, about changes generates distrust in the overall health reform and destabilizes the system in general.

The time limit for implementation by medicines producers of the Good production practice standard, introduced on the territory of the Republic of Bulgaria by way of Ordinance No. 12 of the Ministry of Health, expired on 18 April 2003. After that date producers, who do not satisfy the standards, must terminate their activity. The close down of medicines production workshops is expected to generate tension on the pharmaceutical market, but it is an undeniable fact that the good production practice will open perspectives to Bulgarian medicines producers, strengthen their market positions abroad, and create higher security for the health insured.

Legislation

After the 2002 approval of the Environment Protection Act, the Biodiversity Act, the amendments to the Waters Act, which introduce framework European directives, **the first quarter of 2003 outlined substantially new range of issues concerning the specific application of prescribed environmental norms.** Two new regulations deserve attention within the environmental legislation process.

The new Ordinance on the Terms and Procedure of Conducting Environmental Impact Assessment for Investment Proposals for Construction, Activities, and Technologies treats the application of major provisions of the Environment Protection Act and the Biodiversity Act. It lays down obligations for investors to inform the competent authorities, the mayors and the people concerned, about the parameters of investment proposals - required areas, description of basic production process parameters, type and quantity of expected waste and emissions, proposal implementation alternatives, and to organize preliminary consultations with the persons and organizations concerned with the investment project. On the other hand, the Ordinance regulates the cases in which the Environmental Impact Assessment (EIA) is implemented either by the Ministry of Environment and Water (MEW) or Regional Environmental Inspectorate (REI) authorities. It also lists the obligatory requirements for the scope, content and quality of EIA reports and for the control on the implementation of prescriptions by government authorities.

Ordinance approval is a completion phase of the harmonization of Bulgarian with European legislation in terms of a major instrument of government environmental policy like the EIA. **The transposition of Council Directive 85/337/EC and Council Directive 97/11/EC in this regulation will provide all preconditions to make use of the resources in EU's pre-accession funds allocated for investment projects on the territory of Bulgaria.**

The other document is the **Ordinance on the Terms**

and Procedure of Issuing Integrated Permits for the Construction and Use of New and for the Use of Operating Industrial Plants and Facilities. It regulates the implementation of the provisions of Art. 119, paragraph 1 of the Environment Protection Act on:

- the procedure of issuing integrated permits for the construction and use of new and for the use of operating industrial plants and facilities, for the categories of industrial activities pursuant to Annex No. 4 to the Environment Protection Act;
- the terms and procedure of identifying the best available techniques /BAT/ for certain categories of industrial activities;
- the procedure of integrated permits application and control.

The procedure for issuing integrated permits to big enterprises, which are potential environment polluters, aims at creating optimum conditions to improve the energy efficiency of industrial productions and to reduce the consumption of raw materials and resources by way of introducing and operating industrial plants complying with Europe's best available techniques /BAT/. The technological upgrade of production processes in enterprises involves implementation of measures to reduce harmful emissions, prevent water pollution and reduce the quantity of generated industrial waste.

The scope of this ordinance covers 250 big Bulgarian enterprises in the energy, oil, chemical, leather, food industry, agriculture and mining sectors. The production activity of these enterprises must be placed in compliance with Directive 96/61/EC - IPPC Directive, within the period 2003–2007. The rehabilitation of the oldest plants and facilities of some enterprises should be completed in 2012. Companies, which fail to implement the necessary measures by the end of the transitional period, will have to terminate their activity.

The requirements of Council Directive 96/61/EC, which are transposed in the cited ordinance, will contribute to a favorable environment for the export of Bulgarian production in EU Member States. The

effect of this regulation guarantees harmonization of requirements towards Bulgarian industrial enterprises with those in the European Union in terms of industrial environmental performance. **Overall, the process should equalize environmental production standards of Bulgarian enterprises with those of other EU Member States. Thereby, the operating conditions of Bulgarian and European companies in terms of environmental requirements will be made equal and the prerequisites for dumping of the prices of goods and services they produce will be eliminated.**

Ordinance implementation (the process of issuing integrated permits to 70 Bulgarian enterprises will start in June 2003) generated wide public debate in which opinions of government institutions and business representatives were far from synonymous. The price Bulgarian companies have to pay to cover European environmental standards is a major topic of debate. This issue is very significant for companies because future compliance with environmental standards will be a major condition and guarantee for access to the European market and for elimination of unfair competition both in the country and abroad. The second aspect of this process concerns the level (and often the availability) of opportunities to invest in the technological improvement of enterprises, and the effect of these additional costs on prices and on product competitiveness on the national and international markets, accordingly.

According to MEW's implementing programs developed for the negotiation process on Chapter 22: Environment, the funds required to issue integrated permits to companies amount to BGN 6 billion According to Bulgarian Industrial Association estimates, companies will need investments to the amount of USD 10 billion - they will have to make provisions for these funds to cover Directive requirements and set their obsolete production technologies in compliance with higher environmental requirements.

For the implementation of certain environmental standards it is important for national industry that

maximum transitional periods be set forth in the position of the negotiating team before Chapter 22: Environment is closed. Longer transitional periods will contribute for smoother introduction of advanced technological solutions equally complying with environmental standards, limited investment capacities and other economic indicators of companies' operation (like implementation of measures to improve labor productivity, the quality of corporate management, etc.).

The Bulgarian side has requested so far the following transitional periods.

Initially requested transitional periods:

| | |
|--|----------------|
| Sulfur content of some liquid fuels/Directive 1999/32/EC | Till 1.01.2015 |
| Packaging and packaging waste/Directive 94/62/EC | Till 1.01.2012 |
| Waste depots /Directive 1999/31/EC | Till 1.01.2015 |
| Full prevention and control of industrial pollution/ Directive 96/61/EC | Till 1.01.2012 |
| Town sewage water treatment/Directive 91/271/EEC | Till 1.01.2015 |
| Discharge of dangerous substances in surface water /Directive 76/464/EEC | Till 1.01.2015 |
| Emissions from the use of organic solvents in some activities and installations/Directive 1999/13/EC | Till 1.01.2012 |

Transitional periods requested for new EU legislation:

| | |
|---|-----------------|
| Old motor vehicles/Directive 2000/53/EU | Till 31.12.2011 |
| Big combustion installations /Directive 2001/80/EU: | |
| Varna TPP | Till 31.12.2014 |
| Bobovdol TPP | Till 31.12.2011 |
| Russe - Iztok TPP | Till 31.12.2009 |
| Lukoil Neftochim TPP | Till 31.12.2011 |

Source: MEW http://www.moew.government.bg/recent_doc/

Financing of Environmental Activities

A state-owned **Company for management of environment protection activities** was set up on the strength of the Environment Protection Act and came into operation in the beginning of 2003. Company's financial resources predetermine its limited capacity to finance national-industry-related environmental projects in particular.

The State Company-declared priorities in the

provision of grant aid and interest-free or low-interest loans include:

- environmental investment projects (basically related to municipal programs);
- implementation of non-investment environment protection and rehabilitation projects and activities (environmental campaigns);
- scientific and applied research assigned by the Ministry of Environment and Water;
- development and maintenance of the National Environment and Water Monitoring System and of monitoring and control related activities.

According to MEW's 2002 report, environmental fund assets were basically spent on waste management activities on regional level and on improving the water supply of towns and villages through the construction of small projects of local significance.

According to business representatives, the question of the money, which companies pay to the environmental fund in the form of charges, and of the principle of their disbursement remains open. According to the Bulgarian Industrial Association²¹, 70 per cent of these funds are allocated for municipal environmental projects and thereby private companies cannot get financing for their environmental projects. Industrial trade associations are of the opinion that there is a need to effectively orient the control on the disbursement of funds, which companies pay to the state budget in the form of environmental charges, towards new priorities and to redirect a portion of these funds for promotion of environmental economic projects.

Sector Environmental Policies

Areas, which are increasingly associated with attraction of environmental investments and creating job opportunities through environmental activities include: national geological prospecting and mining, development of environmental tourism and environmental agriculture.

The Ministry of Environment and Water prepares

in cooperation with the Bulgarian Mining Chamber **a proposal for updates and amendments to the Strategy for Development of Geological Prospecting and Protection of Earth's Interior in the Republic of Bulgaria till 2010**. Publication of an Internet Catalogue of the Type and Quality of Bulgaria's Underground Resources is pending. It will help foreign investors to improve their awareness of Bulgaria's geological prospecting and mining sector. According to MEW's data, in 2003 alone companies have been issued 52 licenses for prospecting of metallic and non-metallic mineral resources in different Bulgarian regions.

The bilateral work program signed between the agricultural ministries of Bulgaria and Holland in March 2003 provides an opportunity for Bulgaria to become a beneficiary of the aid under the Global Environmental Fund for development of organic farming in the country. Development of a National Agro-environmental Program was started. It will enable Bulgarian companies to participate with projects for non-repayable financing of activities in the area of biological production and processing of biological products.

In light of the Strategy for Development of Bulgarian Environmental Tourism, MEW initiated the set up of an independent Protected Bulgarian Territories Fund. The fund is envisaged to dispose of around BGN 25 m per year. MEW and MA undertook to provide half of the necessary amount; the other half is expected to come from donors and from revenues accumulated by the fund. Project preparation unites the efforts of the World Bank, USAID, and the governments of Germany, Switzerland and Denmark. The objective of this project is to improve by way of this fund Bulgaria's national biological diversity, to rehabilitate the material resources of national parks, to provide financing for municipal biodiversity projects and environmental tourism development projects in towns and villages in or near protected territories. The fund is expected to come into operation since August 2003.

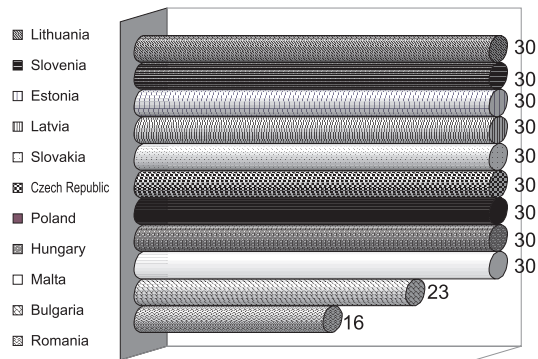
²¹ See. <http://b2billionbia-bg.com/index.asp?i=1959&l=1>

Table 11. Monitoring of negotiations for Bulgaria’s accession to EU

| Chapter | Status (31 March 2003) |
|---------------------------------------|------------------------|
| 1 Free Movement of Goods | temporarily closed |
| 2 Free Movement of Persons | temporarily closed |
| 3 Freedom to Provide Services | temporarily closed |
| 4 Free Movement of Capital | temporarily closed |
| 5 Company Law | temporarily closed |
| 6 Competition Policy | open |
| 7 Agriculture | open |
| 8 Fishery | temporarily closed |
| 9 Transport Policy | closed in May 2003 |
| 10 Tax Policy | temporarily closed |
| 11 Economic and Monetary Union | temporarily closed |
| 12 Statistics | temporarily closed |
| 13 Social Policy | temporarily closed |
| 14 Energy | temporarily closed |
| 15 Industrial Policy | temporarily closed |
| 16 Small and Medium-Sized Enterprises | temporarily closed |
| 17 Science and Research | temporarily closed |
| 18 Education and Training | temporarily closed |
| 19 Telecommunications | temporarily closed |
| 20 Culture and Audiovision | temporarily closed |
| 21 Regional Policy | open |
| 22 Environment | open |
| 23 Consumer Protection | temporarily closed |
| 24 Justice and Home Affairs | open |
| 25 Customs Union | temporarily closed |
| 26 Foreign Relations | temporarily closed |
| 27 Common Foreign and Security Policy | temporarily closed |
| 28 Fiscal Control | temporarily closed |
| 29 Fiscal and Budgetary Issues | open |
| 30 Institutions | temporarily closed |
| Total chapters closed | 23 |

On 1 January 2003 Greece took up the Presidency of the European Union. After the good news at the end of 2002, the new year started with hopes and expectations for accelerated development of the negotiations for accession. But the tense international situation had unfavorable effect. The first three months of 2003 did not prove the best time for development of the negotiations for Bulgaria’s accession to the European Union. The events and the war in Iraq somewhat delayed the negotiations for accession. Bulgaria did not close any new chapter of the negotiations (Figure 24). At the end of March 2003 the Minister of European Affairs and Chief Negotiator expressed a concern that the negotiations with the European Union may well not be completed by the end of May 2004, which is the preliminary target date.

Figure 24. Temporarily closed chapters of negotiations for accession (by candidate countries, as of 31 March 2003)



It is of vital importance for Bulgaria that the European Commission approve the financial framework required to complete the negotiations on the most serious and difficult chapters: Chapter 7: Agriculture; Chapter 21: Regional Policy; and Chapter 29: Fiscal

and Budgetary Issues. The progress to be reported by Bulgaria in the next months is an important factor for the development of negotiations, because it will be reflected in European Commission's Annual Report on the Progress of Bulgaria.

The remaining chapters are conditionally divided in two groups according to expected difficulties - technical and financial.

According to Government estimates, negotiations on the chapters in the first group - Chapter 9: Transport Policy²², Chapter 22: Environment, and Chapter 24: Justice and Home Affairs may be completed by the end of 2003, which is the initially set time-limit. The development of the negotiation process on the chapters in the second group is fully dependable on the European Commission. The latter should approve the financial framework, which is indispensable for closing Chapter 7: Agriculture, Chapter 21: Regional Policy, and Chapter 29: Fiscal and Budgetary Issues.

The financial framework of the European Union is approved for a six-year period. The current budget is made till the year 2006 and covers only the first 10 countries to be officially acceded in 2004. The opinion of the Minister of European Affairs is that "we are ready to quickly complete the negotiations provided that we have this financial perspective to be given on the same principles as to the first ten countries, that is, to be confirmed that we are part of the fifth EU enlargement". Bulgaria requested Brussels not to bind negotiation on fiscal chapters to the next European Community budget for the period 2007 - 2012 when our country is expected to become a full member of the European Union.

It should be noted that if the Regular Report of the European commission on the progress of Bulgaria, to be published in October, does not state that the country is ready to complete the negotiations, that will not happen by the end of May 2004 (which is the Government aim).

Unfortunately there is certain delay in the passing of some important draft laws and ordinances, which has unfavorable effect on the negotiations for accession.

Bulgaria must build up the structures for utilization of the money from European funds and programs by the end of 2004. All government institutions engaged in the programming, monitoring, financial management and control of the aid from EU pre-accession funds must be in place and fully operational. By the end of 2002 Bulgaria utilized under the PHARE Program more than 95 per cent of the funds for 1998 and 1989, and more than 80 per cent of the agreed amount was paid. Nine financial memorandums for realization, five for environment and four in the Transport Sector were signed in 2000 and 2001 under ISPA. In 2002 ISPA's Management Committee approved the financing of 7 projects, which were signed at the end of January 2003. One is in the field of transport and six are in the field of environment. Total value of projects in the two sectors exceeds EUR 908 m, with more than EUR 525.8 m coming from European programs, EUR 216 representing a loan from international financial institutions and over EUR 165.8 m provided from the state budget.

Thereby the Bulgarian Government guarantees utilization within three years (half of the period for ISPA) of around 75 of the funds earmarked under the program for the whole period, with three years remaining for utilization of the other 25 per cent. At the end of 2002 Bulgaria utilized 11 per cent of the funds under ISPA, which ranks the country third according to this indicator (after Poland and Romania). Proposals for projects to be financed under ISPA in the period 2003 - 2004 have been sent to the European Commission in Brussels for approval.

Meanwhile, the **Regular Report of the European Commission on the Economic Situation and Perspectives of Candidate Countries** was published in late March and early April. The European Commission makes positive assessment of their development and states that the unfavorable international economic situation had no effect on

²² Chapter 22: Transport Policy was closed in May

their economic growth. Projections are encouraging for Bulgaria and Romania. Their 2003-2004 growth is estimated at 4.5 - 5 per cent. Risk probability is also projected, given the geopolitical situation, and the persisting high foreign debt is also pointed out for Bulgaria.

The Treaty of Nice formally took effect on 1 February 2003. It regulates the necessary changes in European institutions in relation to the 2004 EU enlargement. The treaty was developed in 2000 at the Intergovernmental Conference during the European Council in Nice in December. This is the fourth amendment of the 1957 Treaty of Rome, which is a fundamental treaty establishing the European Communities. The Treaty of Nice was signed on 26 February 2001, however it required ratification by all Member States to take effect. Basic institutional reforms include:

- New distribution of the votes in the Council of Ministers, ranging from 3 to 29 votes per State. That will allow to take better account of the demographic weight of each State. No agreement may be approved without the consent of the majority of States (in the case of 27 members, 14 States must have voted "for"). Nevertheless, big States like Germany remain privileged. Any State may propose a check of whether the States, which have voted for a decision, represent 62 per cent of the population of the European Union. If that is not the case, the decision shall not be valid.
- The number of deputies in the future European Parliament will be increased from 626 to 732.
- The future European Commission to come into operation in November 2004 will comprise 25 members (one member each from a Member State). Big Member States will not have second commissioner. When the European Union enlarges up to 27 states, the number of commissioners will be less than that of the Member States.
- The number of cases, where decisions are to be taken by qualified majority, is increased.
- The requirement for unanimous vote for

appointment to important positions like Chairman and Members of the European Commission, High Commissioner on Common Foreign and Security Policy, special representatives, and the Deputy General Secretary of the Council is eliminated.

- The Chairman of the European Commission is delegated more powers.
- The Treaty of Nice introduces a new action procedure in the event of established gross violation of fundamental rights by a Member State. The European Council may divest that Member State of some of its rights, the right to a vote in the Council, for example.

At the end of March 2003 Bulgaria signed in Brussels the protocol for joining NATO. In spite of the numerous speculations, the Commissioner on Enlargement Guenter Ferheugen stated that Bulgaria's position on the Iraqi crisis could not have negative effect on the country's accession to the European Union. Regarding the progress of negotiations for accession, Guenter Ferheugen confirmed again that Bulgaria would be judged by its own achievements. But he did not clearly state either that 2007 is the realistic year for Bulgaria's accession. "We have never maintained that. We only say that we support this ambition of Bulgaria, but it is too early to say whether it is realistic."

Hopes remain that Bulgaria will manage to achieve progress and specific understanding on the date for its accession to the European Union. On his return from the 16th Session of the Joint Parliamentary Committee Bulgaria - European Union in Brussels, Bulgarian Minister of Foreign Affairs confirmed that: "negotiations with the European Union become major Government priority, which will absorb most of government's efforts in the next two years... We have gained excellent momentum, which we must use in the negotiations with the European Union. That is why our proposal is to continue and complete negotiations under the most favorable for Bulgaria general conditions, which should be at least as favorable as for the other 10 countries which are acceding now."

Licensing Regimes

The Act on the Administrative Regulation and Administrative Control of Economic Activity was passed on first reading. The objective of this act is to limit the intervention of central and local government in the operations of commercial companies and entrepreneurs. The draft law was developed by a team comprising jurists from ASME, IME, BCCI, BIA, the Economic Policy Commission of the National Assembly, and the Ministry of Economy. According to the authors, the basic advantage of this act is the attempt to conquer the causes and not the effects - its objective is to curb corruption, which is often generated by the absolute power of the administration.

It should be noted, however, that some important texts from the original paper have been dropped in the variant introduced in the National Assembly. These include:

- The requirement for preliminary assessment of the effect of new regulations (licensing regimes) on the economic activity, and the possibility not to introduce some regulations. This formulation was in harmony with provisions and the practice in the EU.
- The requirement for official exchange of information and documents between individual administrative authorities.
- The "tacit agreement" institution in non-expediency regimes (registrations).

According to experts, the deletion of these texts may be explained by the proponent's (Council of Ministers) unwillingness to amend existing provisions, the Administrative Procedure Act in the first place.

Future debates in the National Assembly on second reading will probably be focused precisely on the opportunity to bring these texts back in the act²³.

Public Procurement

The work on the development of an entirely new

Public Procurement Act continues. The special work group set up last year holds its meetings where opportunities to make amendments in the act, targeting higher transparency, flexibility and expediency of procedures, are discussed. Draft completion is expected by 1 July 2003. Some of the proposals, which are being discussed include:

- Set up of a separate public procurement agency in charge of overall public procurement organization and monitoring;
- Improved procedure for appeal by unsuccessful candidates;
- Introduction of standard documents and software obligatory for all contracting authorities;
- Facilitated public procurement regime for the companies in the utilities sector;
- Assigning codes to all orders, compatible with those introduced in the EU;
- Opportunities to introduce preferences for Bulgarian public procurement contractors in the form of 10-per cent discount on the prices they offer;
- Improving the qualification of the commissions preparing public procurement procedures, and giving more clear definition of the administrative and criminal liability of their members;
- Improved Public Procurement Register;
- Accelerated introduction of e-government in its public procurement section.

Protection of Competition

An Act Amending the Act on Protection of Competition (APC) was promulgated in the beginning of 2003. It constitutes profound revision of the legal regulation of competitive relations in the country. Only 10 out of the 60 articles in the act remain unchanged. Three new provisions are introduced, which are of vital importance for the regulation of fair competition in the country. They provide for the following:

- The rights of the Commission for Protection of Competition are expanded, while its statute remains unchanged. Its powers are expanded in terms of conducting sector analyses of the markets, which are most threatened by competitive violations.

²³ The act was passed on second reading in June, with paragraphs on preliminary assessment and "tacit agreement" approved on a proposal by MPs.

- Significant changes have been made with regard to conference agreements. It is envisaged for the Commission to control the observation of the conditions, specified for the parties to the conference agreement upon its individual authorization by the Commission.
- The act also regulates a prohibition for misuse of joint dominating position. In this case subject to sanctions shall be companies having joint dominating position on the market - a market share of 35 per cent, as well as their behavior manifested in direct or indirect setting of selling prices, restriction of production, etc.
- Changes have also been made with regard to economic activity concentration. A single assessment criterion for the significance of planned concentration is introduced – the aggregate turnover of the enterprises affected by the concentration.
- Debates were fanned to a heat around CPC's powers to conduct field checks and to enforce collection of evidence in the offices and working premises of companies. Strong guarantees against misuse by CPC officials are envisaged to that effect.

Amendments to the act will generate amendments of other regulations related to CPC's operation. The accelerated implementation of this process will result in a comprehensive legal framework of competition in Bulgaria. There is a need to launch a wide campaign to explain amendments - that will improve the awareness of entrepreneurs about fair competition rules.

Regulation of Bankruptcy Procedures

In March the National Assembly passed on first reading amendments to the Commercial Code, which basically aim at accelerating bankruptcy procedures and the procedures for transformation of commercial companies. Amendments envisage drastic cut down of the number of procedures and the terms for their execution, as well as better protection of the interests of good faith creditors. Amendments to company law, regulating the procedures for amalgamation, merger, division and separation

in sole proprietor companies, are also envisaged. Powers of shareholders are expanded and a number of changes are introduced in the procedure of holding general meetings and in the required majority for decisions. Amendments to the Code were finally passed in May.

Reform of the Judiciary System

Difficulties and problems in the judiciary system persist, as well as their negative effect on both the business environment and the overall "image" of Bulgaria in the international community and among foreign investors. Problems with judiciary's budget, disputes on the amendments to the Judiciary System Act (the Constitutional Court repealed 44 texts of the Judiciary System Act) also have negative effect on the process of negotiations between Bulgaria and EU on judiciary system issues.

Efforts to implement the reform of the judiciary system through the consensus of parliamentary represented parties continued in the first quarter of 2003.

Political consensus on the basic guidelines of reform and an understanding for amendments to the Constitution, which are executable by the 39 National Assembly, were reached at the end of March. The present Constitution is basically blamed for contributing to a non-operational and poorly structured judiciary system through the absence of a sufficient number of mechanisms for reciprocal control of authorities. Amendments will target improved structure, powers and efficiency of the judiciary system.

The fundamental goals of reform, on which political forces reached a consensus, include:

- Improved mechanisms for coordination and cooperation of the Prosecution, the Investigation, and the Executive;
- Structural and operational changes in the judiciary system;
- Improved operation of the judicial administration;
- Improved material and technical basis of the judiciary system;

- Clear definition of the functions of the Supreme Judicial Council;
- Amendments to the remedial legislation.

In early April the political forces signed a Declaration, which sets a period of one year to make amendments to the Constitution. Thereby the immunity of magistrates will be restricted, that is, magistrates will not be permanent, and chief justices will have mandates. For now, changes in the statute of the Prosecution and the Investigation are not envisaged, as they require a Grand National Assembly.

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|--|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|----|
| Economic dynamics | | | | | | | | | | | | | |
| Industry | | | | | | | | | | | | | |
| Industrial production, volume index, previous month =100, % | | | | | | | | | | | | | |
| 2003 | 86.5 | 96.7 | 114.1 | | | | | | | | | | |
| 2002 | 81.5 | 99.7 | 109.2 | 101.6 | 96.5 | 106.3 | 105.2 | 95.8 | 103.9 | 100.4 | 105.3 | 101.6 | - |
| Industrial production, volume index, corresponding month of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 115.4 | 115.4 | 120.6 | | | | | | | | | | |
| 2002 | 96.6 | 94.2 | 96 | 111.5 | 104.5 | 107.6 | 112 | 104.6 | 109.7 | 105.6 | 109.9 | 104 | - |
| Industrial production, from the beginning of the year, volume index, corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 115.4 | 115.4 | 117.2 | | | | | | | | | | |
| 2002 | 96.6 | 95.4 | 95.6 | 99.3 | 100.3 | 101.5 | 103 | 103.2 | 104 | 104.1 | 104.7 | 104.6 | - |
| Industrial sales, total, volume index, previous month =100, % | | | | | | | | | | | | | |
| 2003 | 86.2 | 96.8 | 117.9 | | | | | | | | | | |
| 2002 | 82.3 | 97.9 | 106.8 | 108.4 | 93 | 108.4 | 107 | 95.5 | 101.9 | 99 | 104.3 | 104.7 | - |
| Industrial sales, total, corresponding month of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 86.2 | 96.8 | 117.9 | | | | | | | | | | |
| 2002 | 82.3 | 97.9 | 106.8 | 108.4 | 93 | 108.4 | 107 | 95.5 | 101.9 | 99 | 104.3 | 104.7 | - |
| Industrial sales, total, A43, volume index, corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 117.8 | 117.1 | 121 | | | | | | | | | | |
| 2002 | 90.7 | 90.2 | 90.3 | 94.7 | 95 | 96.5 | 98.5 | 99.3 | 100.4 | 100.4 | 100.9 | 101.3 | - |
| Domestic trade | | | | | | | | | | | | | |
| Trade and repairing activities, total, net receipts from sales, volume index, previous month =100, % | | | | | | | | | | | | | |
| 2003 | 71 | 102.7 | 107.1 | | | | | | | | | | |
| 2002 | - | 113.3 | 111.7 | 98.9 | 98.2 | 101.6 | 111.6 | 102.4 | 101.4 | 108.3 | 96.6 | 109.5 | - |
| Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, previous month =100, % | | | | | | | | | | | | | |
| 2003 | 76.7 | 98 | 107.3 | | | | | | | | | | |
| 2002 | - | 99.7 | 116.9 | 95.4 | 99.6 | 107.7 | 106.7 | 97 | 102.7 | 107.9 | 101.6 | 102.4 | - |
| Wholesale and commission trade, net receipts from sales, volume index, previous month =100, % | | | | | | | | | | | | | |
| 2003 | 70.2 | 104.1 | 106.7 | | | | | | | | | | |
| 2002 | - | 118.3 | 112 | 99.1 | 97.3 | 100.5 | 113.7 | 103 | 100.9 | 109.3 | 95.4 | 109.9 | - |
| Retail trade, repair of personal and household goods, net receipts from sales, volume index, previous month =100, % | | | | | | | | | | | | | |
| 2003 | 71 | 98.9 | 109.4 | | | | | | | | | | |
| 2002 | - | 100.8 | 106.4 | 100.1 | 101.7 | 102.6 | 105.1 | 103.3 | 102.9 | 103.7 | 99.6 | 112.6 | - |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|---|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-----|
| Trade and repairing activities, total, net receipts from sales, volume index, corresponding month of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 106.1 | 107.2 | 108.1 | | | | | | | | | | |
| 2002 | 93.1 | 100.1 | 97.9 | 103 | 100.1 | 101.9 | 106.6 | 108.9 | 110.6 | 109.5 | 109 | 111.1 | - |
| Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, corresponding month of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 103.5 | 98.8 | 100.6 | | | | | | | | | | |
| 2002 | 97.3 | 106.7 | 103.1 | 103.1 | 98.4 | 98.5 | 98.7 | 98.9 | 101.4 | 102.9 | 105.3 | 104.7 | - |
| Wholesale and commission trade, net receipts from sales, volume index, corresponding month of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 107.5 | 109.5 | 109.8 | | | | | | | | | | |
| 2002 | 90.9 | 98.7 | 96.4 | 103.2 | 100.3 | 102.6 | 108.3 | 110.9 | 113.5 | 111.6 | 110.8 | 113.4 | - |
| Retail trade, repair of personal and household goods, net receipts from sales, volume index, corresponding month of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 102 | 102.1 | 104.4 | | | | | | | | | | |
| 2002 | 101 | 103.4 | 101.6 | 101.9 | 100.2 | 101.1 | 104.5 | 106.2 | 104.1 | 103.7 | 103.3 | 104.9 | - |
| Trade and repairing activities, total, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 106.1 | 107.8 | 108 | | | | | | | | | | |
| 2002 | 93.1 | 96.7 | 95.4 | 97.3 | 97.9 | 98.5 | 99.8 | 101 | 102.1 | 102.9 | 103.5 | 104.3 | - |
| Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 103.5 | 101.5 | 101.2 | | | | | | | | | | |
| 2002 | 97.3 | 101.8 | 102.3 | 102.5 | 101.6 | 101 | 100.7 | 100.4 | 100.5 | 100.8 | 101.3 | 101.7 | - |
| Wholesale and commission trade, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 107.5 | 109.7 | 110 | | | | | | | | | | |
| 2002 | 90.9 | 94.9 | 93.2 | 95.7 | 96.6 | 97.6 | 99.2 | 100.7 | 102.2 | 103.2 | 104 | 104.9 | - |
| Retail trade, repair of personal and household goods, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 102 | 102.6 | 103.3 | | | | | | | | | | |
| 2002 | 101 | 102.3 | 102.1 | 102.1 | 101.7 | 101.6 | 102 | 102.6 | 102.8 | 102.9 | 102.9 | 103.2 | - |
| Inflation | | | | | | | | | | | | | |
| Inflation (Consumer price index - 100), previous month = 100, % | | | | | | | | | | | | | |
| 2003 | 0.6 | 0.1 | 0.4 | 0.3 | | | | | | | | | |
| 2002 | 2.7 | 1.6 | 0.8 | -0.1 | -2.1 | -1.7 | 0.1 | -0.7 | 0.8 | 1 | 0.2 | 1.2 | - |
| Inflation (Consumer price index - 100), December of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 0.6 | 0.8 | 1.2 | 1.5 | | | | | | | | | |
| 2002 | 2.7 | 4.4 | 5.2 | 5.1 | 2.9 | 1.1 | 1.2 | 0.6 | 1.4 | 2.4 | 2.5 | 3.8 | - |
| Inflation (Consumer price index - 100), corresponding period of the previous year = 100, % | | | | | | | | | | | | | |
| 2003 | 1.7 | 0.2 | -0.2 | 0.2 | | | | | | | | | 0.6 |
| 2002 | 7.0 | 8.4 | 9.2 | 9.2 | 6.9 | 5.2 | 5.5 | 4.5 | 4.0 | 3.2 | 3.2 | 3.8 | 8.2 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| Employment and unemployment | | | | | | | | | | | | Q1 |
|--|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Unemployed persons registered, total, end of the period, number | | | | | | | | | | | | |
| 2003 | 646 700 | 611 727 | 581 350 | 552 068 | | | | | | | | 581 350 |
| 2002 | 687 805 | 683 894 | 668 972 | 678 637 | 673 803 | 659 032 | 653 329 | 650 018 | 644 718 | 644 298 | 624 946 | 668 972 |
| Unemployment (Employment Agency, ratio to the economically active population from the population census in 2001), end of the period, % | | | | | | | | | | | | |
| 2003 | 17.4 | 16.51 | 15.7 | 14.9 | | | | | | | | 15.7 |
| 2002 | 18.57 | 18.46 | 18.06 | 18.32 | 18.19 | 17.79 | 17.64 | 17.55 | 17.4 | 17.39 | 16.87 | 18.06 |
| Newly opened vacant jobs, end of the period, number | | | | | | | | | | | | |
| 2003 | 1 759 | 2 024 | 2 136 | 2 480 | | | | | | | | 2 136 |
| 2002 | 1 588 | 4 177 | 3 284 | 3 420 | 2 437 | 2 055 | 2 011 | 3 272 | 2 802 | 2 270 | 2 651 | 3 284 |
| Employed person, total, end of the period, number | | | | | | | | | | | | |
| 2003 | 1 939 285 | 1 987 936 | 2 013 227 | 1 895 911 | 1 905 823 | 1 913 121 | 1 917 999 | 1 914 477 | 1 925 092 | 1 917 214 | 1 918 643 | 2 013 227 |
| 2002 | 1 878 628 | 1 883 392 | 1 890 173 | 1 895 911 | 1 905 823 | 1 913 121 | 1 917 999 | 1 914 477 | 1 925 092 | 1 917 214 | 1 918 643 | 1 890 173 |
| Employed person, public sector, end of the period, number | | | | | | | | | | | | |
| 2003 | 735 719 | 761 917 | 770 504 | 749 826 | 745 729 | 743 092 | 737 200 | 735 424 | 740 543 | 735 825 | 747 422 | 770 504 |
| 2002 | 761 630 | 762 192 | 760 562 | 749 826 | 745 729 | 743 092 | 737 200 | 735 424 | 740 543 | 735 825 | 747 422 | 760 562 |
| Employed person, private sector, end of the period, number | | | | | | | | | | | | |
| 2003 | 1 203 566 | 1 226 019 | 1 242 723 | 1 146 085 | 1 160 094 | 1 170 029 | 1 180 799 | 1 179 053 | 1 184 549 | 1 181 389 | 1 171 221 | 1 242 723 |
| 2002 | 1 116 998 | 1 121 200 | 1 129 611 | 1 146 085 | 1 160 094 | 1 170 029 | 1 180 799 | 1 179 053 | 1 184 549 | 1 181 389 | 1 171 221 | 1 129 611 |
| Fiscal review | | | | | | | | | | | | |
| State budget, from the beginning of the year | | | | | | | | | | | | |
| Revenues of the Consolidated State Budget, total, BGN million | | | | | | | | | | | | |
| 2003 | 1 029.20 | 1 944.80 | 3 220.60 | 4 040.80 | 5 156.10 | 6 064.40 | 7 247.70 | 8 194.70 | 9 180.60 | 10 312.30 | 11 315.30 | 3 220.6 |
| 2002 | 889.1 | 1 752.70 | 2 782.30 | 4 040.80 | 5 156.10 | 6 064.40 | 7 247.70 | 8 194.70 | 9 180.60 | 10 312.30 | 11 315.30 | 2 782.3 |
| Expenditures of the Consolidated State Budget, total, BGN million | | | | | | | | | | | | |
| 2003 | 1 130.60 | 2 105.40 | 3 109.80 | 3 928.60 | 4 816.50 | 5 733.60 | 6 843.60 | 7 778.00 | 8 688.80 | 9 667.10 | 10 789.50 | 3 109.8 |
| 2002 | 1 020.30 | 1 905.90 | 2 821.10 | 3 928.60 | 4 816.50 | 5 733.60 | 6 843.60 | 7 778.00 | 8 688.80 | 9 667.10 | 10 789.50 | 2 821.1 |
| Consolidated State Budget deficit (-)/surplus (+), BGN million | | | | | | | | | | | | |
| 2003 | -101.5 | -160.6 | 110.8 | 112.2 | 339.6 | 330.8 | 404.1 | 416.7 | 491.8 | 645.2 | 525.8 | 110.8 |
| 2002 | -131.2 | -153.2 | -38.8 | 112.2 | 339.6 | 330.8 | 404.1 | 416.7 | 491.8 | 645.2 | 525.8 | -38.8 |
| Revenues of the Republican Budget, total, BGN million | | | | | | | | | | | | |
| 2003 | 651.3 | 908.4 | 1 937.00 | 2 364.30 | 3 042.60 | 3 540.50 | 4 242.30 | 4 783.10 | 5 355.40 | 6 076.40 | 6 647.00 | 1 937.0 |
| 2002 | 521.9 | 985.5 | 1 585.00 | 2 364.30 | 3 042.60 | 3 540.50 | 4 242.30 | 4 783.10 | 5 355.40 | 6 076.40 | 6 647.00 | 1 585.0 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|--|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|---------|
| Expenditures of the Republican Budget, total, BGN million | | | | | | | | | | | | | |
| 2003 | 737 | 1 195.60 | 1 846.20 | | | | | | | | | | 1 846.2 |
| 2002 | 367.7 | 869.5 | 1 376.10 | 2 113.10 | 2 531.40 | 3 018.50 | 3 718.50 | 4 205.20 | 4 697.00 | 5 252.80 | 5 949.20 | 7 286.00 | 1 376.1 |
| Republican Budget cash deficit (-) / surplus (+), BGN million | | | | | | | | | | | | | |
| 2003 | -85.7 | -287.2 | 90.8 | | | | | | | | | | 90.8 |
| 2002 | 154.2 | 116 | 208.9 | 251.3 | 511.1 | 521.9 | 523.8 | 577.9 | 658.4 | 823.5 | 697.8 | 3.4 | 208.9 |
| Government and government guaranteed debt | | | | | | | | | | | | | |
| Government and government guaranteed debt, BGN million | | | | | | | | | | | | | |
| 2003 | 17 547.90 | 17 638.70 | 17 560.20 | | | | | | | | | | 17 560 |
| 2002 | 20 993.00 | 20 917.30 | 20 859.00 | 20 103.20 | 19 502.20 | 18 855.30 | 18 992.50 | 18 963.90 | 18 928.70 | 18 666.60 | 18 626.50 | 18 180.20 | 20 859 |
| Domestic government and government guaranteed debt, BGN million | | | | | | | | | | | | | |
| 2003 | 2 113.50 | 1 128.60 | 2 290.70 | | | | | | | | | | 2 291 |
| 2002 | 1 897.00 | 1 889.90 | 1 917.20 | 1 926.70 | 1 907.90 | 1 949.20 | 1 973.00 | 1 987.70 | 2 029.60 | 2 041.90 | 2 087.70 | 2 111.70 | 1 917 |
| Foreign government and government guaranteed debt, BGN million | | | | | | | | | | | | | |
| 2003 | 15 434.40 | 15 431.30 | 15 269.80 | | | | | | | | | | 15 270 |
| 2002 | 19 096.00 | 19 027.40 | 18 941.80 | 18 176.50 | 17 594.30 | 16 906.10 | 17 019.50 | 16 976.20 | 16 899.20 | 16 624.70 | 16 538.90 | 16 068.50 | 18 942 |
| Government and government guaranteed debt, ratio to the annual GDP, % | | | | | | | | | | | | | |
| 2003 | 49.7 | 50.0 | 49.8 | | | | | | | | | | 49.8 |
| 2002 | 68.2 | 68.0 | 67.6 | 65.3 | 63.4 | 61.3 | 61.8 | 61.6 | 61.5 | 60.6 | 60.5 | 56.0 | 67.6 |
| Domestic government and government guaranteed debt, ratio to the annual GDP, % | | | | | | | | | | | | | |
| 2003 | 6.0 | 6.3 | 6.5 | | | | | | | | | | 6.5 |
| 2002 | 6.2 | 6.1 | 6.2 | 6.3 | 6.2 | 6.3 | 6.4 | 6.5 | 6.6 | 6.6 | 6.8 | 6.5 | 6.2 |
| Foreign government and government guaranteed debt, ratio to the annual GDP, % | | | | | | | | | | | | | |
| 2003 | 43.7 | 43.7 | 43.3 | 59.0 | 57.2 | 55.0 | 55.4 | 55.2 | 54.9 | 54.0 | 53.7 | 49.5 | 43.3 |
| 2002 | 62.0 | 61.8 | 61.4 | | | | | | | | | | 61.4 |
| Domestic government debt, total, BGN million | | | | | | | | | | | | | |
| 2003 | 2 111.60 | 2 205.80 | 2 289.40 | | | | | | | | | | 2 289 |
| 2002 | 1 890.60 | 1 883.90 | 1 911.60 | 1 921.60 | 1 903.40 | 1 945.30 | 1 973.00 | 1 987.70 | 2 026.60 | 2 039.30 | 2 085.40 | 2 109.80 | 1 912 |
| Debt on Government Securities issued for budget deficit financing, BGN million | | | | | | | | | | | | | |
| 2003 | 1 515.40 | 1 608.50 | 1 696.00 | | | | | | | | | | 1 696 |
| 2002 | 1 144.40 | 1 138.80 | 1 172.00 | 1 197.60 | 1 201.00 | 1 268.50 | 1 285.80 | 1 307.20 | 1 350.70 | 1 369.30 | 1 418.00 | 1 462.20 | 1 172 |
| Debt on Government Securities issued for structural reform, BGN million | | | | | | | | | | | | | |
| 2003 | 596.2 | 597.2 | 593.4 | | | | | | | | | | 593 |
| 2002 | 746.1 | 745.1 | 739.6 | 724.1 | 702.4 | 676.8 | 683.5 | 677.1 | 675.9 | 669.9 | 667.3 | 647.6 | 740 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|--|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|---------|
| Domestic government guarantees, BGN million | | | | | | | | | | | | | |
| 2003 | 1.8 | 1.5 | 1.2 | | | | | | | | | | 1.2 |
| 2002 | 6.4 | 6 | 5.6 | 5.1 | 4.5 | 3.9 | 3.7 | 3.3 | 3 | 2.6 | 2.3 | 1.9 | 5.6 |
| Foreign government debt, USD million | | | | | | | | | | | | | |
| 2003 | 8 109.30 | 8 091.60 | 8 090.00 | | | | | | | | | | 8 090 |
| 2002 | 7 925.10 | 7 920.70 | 7 920.90 | 7 840.00 | 7 936.00 | 8 103.20 | 7 997.10 | 7 996.50 | 7 967.30 | 7 848.70 | 7 861.50 | 7 978.40 | 7 921 |
| Foreign government guaranteed debt, USD million | | | | | | | | | | | | | |
| 2003 | 426.3 | 415.3 | 416 | | | | | | | | | | 416 |
| 2002 | 507.8 | 495.5 | 503.2 | 504.7 | 508.7 | 529.1 | 524.2 | 538.3 | 541.2 | 535.8 | 533 | 546.2 | 503 |
| Foreign economic relations and foreign investments | | | | | | | | | | | | | |
| Balance of Payments | | | | | | | | | | | | | |
| Current account, USD million | | | | | | | | | | | | | |
| 2003 | -157.5 | -151.3 | -82.2 | | | | | | | | | | -391.0 |
| 2002 | -130.4 | -51.9 | -55.2 | -137.2 | -101.3 | 93.1 | 116.3 | 160.6 | 51 | -141.2 | -179.3 | -301.9 | -237.5 |
| Exports (FOB), USD million | | | | | | | | | | | | | |
| 2003 | 543.1 | 530.9 | 635.1 | | | | | | | | | | 1 709.2 |
| 2002 | 383.7 | 408.8 | 408.0 | 425.4 | 402.9 | 496.4 | 586.3 | 525.6 | 527.6 | 520.2 | 527.3 | 475.6 | 1 200.5 |
| Imports (FOB), USD million | | | | | | | | | | | | | |
| 2003 | 614.4 | 655.8 | 753.8 | | | | | | | | | | 2 024.0 |
| 2002 | 466.1 | 484.1 | 502.1 | 573.8 | 592.7 | 570 | 668.5 | 582 | 609.3 | 694.2 | 736.1 | 801.4 | 1 452.4 |
| Trade balance, (FOB), USD million | | | | | | | | | | | | | |
| 2003 | -71.3 | -124.8 | -118.7 | | | | | | | | | | -314.8 |
| 2002 | -82.4 | -75.4 | -94.1 | -148.4 | -189.8 | -73.7 | -82.2 | -56.5 | -81.7 | -173.9 | -208.8 | -325.9 | -251.9 |
| Capital account, USD million | | | | | | | | | | | | | |
| 2003 | 0 | 0 | 0 | | | | | | | | | | 0 |
| 2002 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Financial account, USD million | | | | | | | | | | | | | |
| 2003 | -65.5 | 22.6 | 53.5 | | | | | | | | | | 10.6 |
| 2002 | 46.1 | 10.2 | 55.4 | 274.9 | 221 | 127.9 | -146.3 | 3 | 121.9 | 176.9 | 188.5 | 173.5 | 111.7 |
| Direct investment in Bulgaria, USD million | | | | | | | | | | | | | |
| 2003 | 41.5 | 32.6 | 107.4 | | | | | | | | | | 181.5 |
| 2002 | 20.3 | 29.7 | 76.3 | 83.4 | 36 | -16.3 | -23.4 | 23.4 | 24.7 | 116.3 | 42.3 | 66.2 | 126.3 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| Finance | | | | | | | | | | | | | |
|--|-----------|-----------|-----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|-----------|
| Financial indicators | | | | | | | | | | | | | |
| Exchange rate BGN / USD, average for the period | | | | | | | | | | | | | |
| 2003 | 1.8417 | 1.81554 | 1.81026 | 1.80353 | 2.13121 | 2.04781 | 1.97152 | 2.00039 | 1.99537 | 1.99354 | 1.95327 | 1.92447 | 1.82250 |
| 2002 | 2.21474 | 2.24804 | 2.23369 | 2.20959 | 2.08355 | 1.96073 | 1.99921 | 1.98905 | 1.9836 | 1.9828 | 1.97021 | 1.88496 | 2.23216 |
| Exchange rate BGN / USD, end of the period | | | | | | | | | | | | | |
| 2003 | 1.80827 | 1.81393 | 1.79516 | 1.7571 | 2.08355 | 1.96073 | 1.99921 | 1.98905 | 1.9836 | 1.9828 | 1.97021 | 1.88496 | 1.79516 |
| 2002 | 2.26448 | 2.26081 | 2.2419 | 2.17121 | 2.08355 | 1.96073 | 1.99921 | 1.98905 | 1.9836 | 1.9828 | 1.97021 | 1.88496 | 2.24190 |
| Basic interest rate, effective annual, average for the period | | | | | | | | | | | | | |
| 2003 | 3.27 | 2.53 | 2.55 | 2.60 | 3.98 | 3.79 | 3.72 | 3.82 | 3.81 | 3.76 | 3.76 | 3.39 | 2.78 |
| 2002 | 4.86 | 4.66 | 4.52 | 4.16 | 3.98 | 3.79 | 3.72 | 3.82 | 3.81 | 3.76 | 3.76 | 3.39 | 4.68 |
| Money (M1), BGN million | | | | | | | | | | | | | |
| 2003 | 5 142.6 | 5 236.6 | 5 089.2 | 4 602.9 | 4 474.8 | 4 402.9 | 4 589.0 | 4 750.4 | 4 804.9 | 4 804.1 | 4 936.0 | 5 542.7 | 5089.2 |
| 2002 | 4 651.4 | 4 584.3 | 4 594.2 | 4 602.9 | 4 474.8 | 4 402.9 | 4 589.0 | 4 750.4 | 4 804.9 | 4 804.1 | 4 936.0 | 5 542.7 | 4594.2 |
| Money (M2), BGN million | | | | | | | | | | | | | |
| 2003 | 13 269.0 | 13 421.2 | 13 192.2 | 12 136.0 | 11 902.6 | 11 875.7 | 12 243.5 | 12 521.5 | 12 589.7 | 12 703.6 | 12 929.4 | 13 581.3 | 13192.2 |
| 2002 | 12 035.3 | 12 068.5 | 12 088.1 | 12 136.0 | 11 902.6 | 11 875.7 | 12 243.5 | 12 521.5 | 12 589.7 | 12 703.6 | 12 929.4 | 13 581.3 | 12088.1 |
| International reserves of BNB, BGN million | | | | | | | | | | | | | |
| 2003 | 8 363.2 | 8 472.8 | 8 602.7 | 7 427.8 | 7 546.3 | 7 908.4 | 8 034.3 | 8 231.8 | 8 496.2 | 8 750.6 | 8 923.6 | 8 947.5 | 8602.7 |
| 2002 | 7 372.4 | 7 373.0 | 7 196.2 | 7 427.8 | 7 546.3 | 7 908.4 | 8 034.3 | 8 231.8 | 8 496.2 | 8 750.6 | 8 923.6 | 8 947.5 | 7196.2 |
| Fiscal reserves at the Issue Department of BNB, BGN million | | | | | | | | | | | | | |
| 2003 | 2 851.6 | 2 860.2 | 3 086.8 | 3 659.7 | 2 803.3 | 3 020.8 | 3 065.5 | 3 108.2 | 3 238.9 | 3 482.0 | 3 685.8 | 3 034.7 | 3086.8 |
| 2002 | 2 276.2 | 2 260.4 | 2 106.5 | 2 358.9 | 2 803.3 | 3 020.8 | 3 065.5 | 3 108.2 | 3 238.9 | 3 482.0 | 3 685.8 | 3 034.7 | 2106.5 |
| Banking system | | | | | | | | | | | | | |
| Claims on credits granted by the Commercial Banks, total, BGN thousand | | | | | | | | | | | | | |
| 2003 | 6 444 818 | 6 563 094 | 6 816 731 | 4796653 | 4944889 | 5065015 | 5352435 | 5512677 | 5765237 | 5923656 | 6126486 | 6409070 | 6 816 731 |
| 2002 | 4 520 277 | 4 543 750 | 4 609 974 | 4796653 | 4944889 | 5065015 | 5352435 | 5512677 | 5765237 | 5923656 | 6126486 | 6409070 | 4 609 974 |
| Credits to Resident Sector, total | | | | | | | | | | | | | |
| 2003 | 6 356 088 | 6 489 685 | 6 745 432 | 4760548 | 4893417 | 5016555 | 5300222 | 5453859 | 5689755 | 5822181 | 6016990 | 6316911 | 6 745 432 |
| 2002 | 4 472 243 | 4 507 846 | 4 573 470 | 4760548 | 4893417 | 5016555 | 5300222 | 5453859 | 5689755 | 5822181 | 6016990 | 6316911 | 4 573 470 |
| Credits to Government Sector | | | | | | | | | | | | | |
| 2003 | 8 673 | 8 947 | 9 494 | 6669 | 6933 | 6512 | 6196 | 9203 | 9404 | 9391 | 9536 | 8486 | 9 494 |
| 2002 | 5 066 | 6 350 | 6 932 | 6669 | 6933 | 6512 | 6196 | 9203 | 9404 | 9391 | 9536 | 8486 | 6 932 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|--|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|-----------|
| Credits to Non-government Sector | | | | | | | | | | | | | |
| 2003 | 6 291 902 | 6 444 224 | 6 662 728 | | | | | | | | | | 6 662 728 |
| 2002 | 4 439 405 | 4 487 627 | 4 552 367 | 4736963 | 4857929 | 4971905 | 5256205 | 5399240 | 5639343 | 5772922 | 5977063 | 6250741 | 4 552 367 |
| Credits to Non-financial Public Corporations | | | | | | | | | | | | | |
| 2003 | 219 215 | 229 954 | 235 631 | | | | | | | | | | 235 631 |
| 2002 | 183 596 | 175 571 | 180 510 | 225524 | 222297 | 211154 | 211675 | 208075 | 195975 | 202831 | 207660 | 215935 | 180 510 |
| Credits to Non-financial Private Corporations | | | | | | | | | | | | | |
| 2003 | 4 715 900 | 4 800 569 | 4 949 708 | | | | | | | | | | 4 949 708 |
| 2002 | 3 339 231 | 3 380 809 | 3 416 763 | 3521944 | 3614751 | 3702339 | 3941157 | 4040047 | 4235802 | 4315476 | 4459918 | 4700997 | 3 416 763 |
| Credits to Households | | | | | | | | | | | | | |
| 2003 | 1 260 492 | 1 300 495 | 1 355 073 | | | | | | | | | | 1 355 073 |
| 2002 | 864 317 | 879 057 | 900 932 | 933388 | 955478 | 993405 | 1035501 | 1079306 | 1126596 | 1172289 | 1214409 | 1241560 | 900 932 |
| Credits to Non-bank Financial Institutions | | | | | | | | | | | | | |
| 2003 | 96 295 | 113 206 | 122 316 | | | | | | | | | | 122 316 |
| 2002 | 52 261 | 52 190 | 54 162 | 56107 | 65403 | 65007 | 67872 | 71812 | 80970 | 82326 | 95076 | 92249 | 54 162 |
| Credits to Resident Banks | | | | | | | | | | | | | |
| 2003 | 55 513 | 36 514 | 73 210 | | | | | | | | | | 73 210 |
| 2002 | 27 772 | 13 869 | 14 171 | 16916 | 28555 | 38138 | 37821 | 45416 | 41008 | 39868 | 30391 | 57684 | 14 171 |
| Credits to Non-resident Sector | | | | | | | | | | | | | |
| 2003 | 88 730 | 73 409 | 71 299 | | | | | | | | | | 71 299 |
| 2002 | 48 034 | 35 904 | 36 504 | 36105 | 51472 | 48460 | 52213 | 58818 | 75482 | 101475 | 109496 | 92159 | 36 504 |
| Total assets, end of the period, BGN thousand | | | | | | | | | | | | | |
| 2003 | 14 470 798 | 14 527 980 | 14 976 602 | | | | | | | | | | 14976602 |
| 2002 | 12 340 044 | 12 286 166 | 12 710 381 | 12 722 090 | 12 473 976 | 12 394 798 | 12 924 968 | 13 225 015 | 13 475 455 | 13 503 015 | 13 901 329 | 14 557 124 | 12710381 |
| Total liabilities, end of the period, BGN thousand | | | | | | | | | | | | | |
| 2003 | 12 413 277 | 12 474 347 | 12 882 639 | | | | | | | | | | 12882639 |
| 2002 | 10 676 646 | 10 602 225 | 11 014 662 | 11 040 181 | 10 782 330 | 10 682 602 | 11 197 870 | 11 455 975 | 11 681 572 | 11 674 854 | 12 053 348 | 12 621 459 | 11014662 |
| Interest revenues, BGN thousand | | | | | | | | | | | | | |
| 2003 | 74 730 | 145 393 | 223 314 | | | | | | | | | | 223314 |
| 2002 | 56 711 | 110 773 | 168 685 | 224 465 | 283 518 | 342 850 | 405 735 | 488 644 | 533 137 | 600 091 | 672 166 | 738 092 | 168685 |
| Current profit/loss, BGN thousand | | | | | | | | | | | | | |
| 2003 | 98 482 | 122 770 | 125 420 | | | | | | | | | | 125420 |
| 2002 | 25 913 | 47 270 | 56 996 | 80 116 | 112 082 | 132 715 | 148 229 | 182 185 | 201 740 | 240 089 | 258 199 | 266 625 | 56996 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

Social policy and industrial relations

Wage&Salary 1)

| | | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|---|--|-----|-----|-----|------|------|------|-----|------|-----|-----|-----|-----|-----|
| Average Monthly Wage&Salary of employees under labor contract, total, nominal, BGN | | 270 | 265 | 280 | | | | | | | | | | |
| 2003 | | 270 | 265 | 280 | | | | | | | | | | 272 |
| 2002 | | 251 | 252 | 265 | 262 | 269 | 265 | 267 | 265 | 272 | 271 | 272 | 282 | 256 |
| Average Monthly Wage&Salary of employees under labor contract, public sector, nominal, BGN | | | | | | | | | | | | | | |
| 2003 | | 308 | 298 | 324 | | | | | | | | | | 310 |
| 2002 | | 282 | 285 | 304 | 298 | 318 | 311 | 309 | 312 | 328 | 321 | 319 | 332 | 290 |
| Average Monthly Wage&Salary of employees under labor contract, private sector, nominal, BGN | | | | | | | | | | | | | | |
| 2003 | | 247 | 244 | 253 | | | | | | | | | | 248 |
| 2002 | | 229 | 229 | 238 | 238 | 236 | 235 | 240 | 236 | 237 | 240 | 241 | 249 | 232 |
| Real Average Monthly Wage&Salary of employees under labor contract, total, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | | |
| 2003 | | 5.7 | 4.9 | 5.8 | | | | | | | | | | 5.5 |
| 2002 | | 1.6 | 2.0 | 1.6 | -3.3 | -0.9 | -0.8 | 1.6 | 2.3 | 2.2 | 3.8 | 3.4 | 0.6 | 1.7 |
| Real Average Monthly Wage&Salary of employees under labor contract, public sector, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | | |
| 2003 | | 7.3 | 4.3 | 6.7 | | | | | | | | | | 6.1 |
| 2002 | | 2.6 | 3.5 | 2.8 | -2.9 | -0.8 | 0.2 | 2.1 | 5.2 | 2.8 | 8.3 | 5.5 | 1.2 | 3.0 |
| Real Average Monthly Wage&Salary of employees under labor contract, private sector, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | | |
| 2003 | | 6.0 | 6.3 | 6.5 | | | | | | | | | | 6.3 |
| 2002 | | 1.4 | 1.6 | 1.9 | -2.3 | -0.6 | -0.7 | 2.5 | 0.8 | 3.1 | 1.1 | 2.0 | 0.8 | 1.6 |

Income and consumption of the households 1)

| | | | | | | | | | | | | | | |
|--|--|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|-------|
| Total income, monthly, average per person, nominal, BGN | | | | | | | | | | | | | | |
| 2003 | | 128.82 | 122.39 | 135.79 | | | | | | | | | | 129.0 |
| 2002 | | 113.4 | 113.2 | 126.5 | 130.6 | 136.58 | 135.34 | 137.34 | 142.68 | 148.45 | 146.73 | 144.13 | 195.49 | 117.7 |
| Cash income, monthly, average per person, nominal, BGN | | | | | | | | | | | | | | |
| 2003 | | 124.46 | 118.32 | 130.16 | | | | | | | | | | 124.3 |
| 2002 | | 109.3 | 109.6 | 120.9 | 122.04 | 123.12 | 123.5 | 124.76 | 128.71 | 135.47 | 132.21 | 126.26 | 157.04 | 113.3 |
| Total expenditure, monthly, average per person, nominal, BGN | | | | | | | | | | | | | | |
| 2003 | | 125.16 | 116.02 | 130.11 | | | | | | | | | | 123.8 |
| 2002 | | 109.4 | 112 | 120.3 | 124.05 | 136.42 | 130.59 | 133.61 | 140.79 | 147.64 | 143.62 | 141.58 | 183.83 | 113.9 |
| Cash expenditure, monthly, average per person, nominal, BGN | | | | | | | | | | | | | | |
| 2003 | | 121.08 | 112.26 | 124.88 | | | | | | | | | | 119.4 |
| 2002 | | 105.5 | 108.6 | 114.9 | 115.64 | 123.21 | 118.91 | 121.21 | 126.98 | 134.92 | 129.79 | 124.17 | 146.31 | 109.7 |

ANNEX 1: MAIN INDICATORS FOR THE FIRST QUARTER OF 2003

| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII | Q1 |
|--|------|-----|-----|------|-----|-----|-----|------|------|------|------|------|-----|
| Real total income, monthly, average per person, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | |
| 2003 | 11.6 | 7.9 | 7.5 | | | | | | | | | | 8.9 |
| 2002 | 0.1 | 5.3 | 3.3 | 1.7 | 4.5 | 5.2 | 5.2 | 8.5 | 12.6 | 12.7 | 10.2 | 23.4 | 2.9 |
| Real cash income, monthly, average per person, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | |
| 2003 | 11.9 | 7.7 | 7.8 | | | | | | | | | | 9.1 |
| 2002 | 0.6 | 5.2 | 3.7 | 2.5 | 3.8 | 5.0 | 5.3 | 8.5 | 13.5 | 12.1 | 9.2 | 20.3 | 3.2 |
| Real total expenditure, monthly, average per person, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | |
| 2003 | 12.4 | 3.3 | 8.3 | | | | | | | | | | 8.0 |
| 2002 | -2.5 | 8.3 | 2.9 | -0.3 | 5.3 | 7.7 | 5.5 | 9.8 | 12.3 | 11.5 | 12.5 | 20.2 | 2.8 |
| Real cash expenditure, monthly, average per person, growth, corresponding period of the previous year =100, % | | | | | | | | | | | | | |
| 2003 | 12.8 | 3.1 | 8.9 | | | | | | | | | | 8.2 |
| 2002 | -2.1 | 8.5 | 3.4 | 0.4 | 4.5 | 7.8 | 5.9 | 9.9 | 13.3 | 11.2 | 12.1 | 16.9 | 3.1 |

1) Average monthly values by quarter are calculated as simple average of monthly per capita values.

Sources: Employment Agency, Bulgarian National Bank, Ministry of Finance, National Statistical Institute and own calculations.

Acronyms:

GDP = Gross domestic product

" - " = Not applicable or missing data

ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FIRST QUARTER OF 2003

| Title | Status | Official Gazette |
|---|---------|-------------------|
| ORDINANCE No. 26/17.12.2002 on Determining the List of Illnesses, for which Outpatient Treatment is Fully or Partially Payable by NHIF | New | NO. 1/3.01.2003 |
| ORDINANCE No. 27/17.12.2002 on Determining the Basic Package of Health Services Guaranteed from NHIF's Budget | New | NO. 1/3.01.2003 |
| ORDINANCE No. 9/19.12.2002 on Assessment and Classification of Risk Exposures of Banks and on Making Provisions for Depreciation Losses | New | NO. 2/7.01.2003 |
| ACT on 2003 State Budget of the Republic Of Bulgaria (07.01.2003) | Amended | NO. 2/7.01.2003 |
| ORDINANCE No.15/2001 on the Terms and Procedure of Providing Financial Grant for Development and Diversification of Economic Activities, Providing Opportunities for Multilateral Activities and Alternative Income under EU Special Pre-accession Program for Development of Agriculture and Bulgarian Rural Regions | Amended | NO. 4/14.01.2003 |
| Classified Information Protection ACT (17.01.2003) | Amended | NO. 5/17.01.2003 |
| DECREE No.6/17.1.2003 on Defining the Ceiling Price of Heating Energy for Household Needs Supplied by Heat Distribution Companies Subsidized from the State Budget | New | NO. 6/21.01.2003 |
| Mandatory Social Security CODE | Amended | NO. 8/28.01.2003 |
| Financial Supervision Commission ACT | New | NO. 8/28.01.2003 |
| Supplementary Voluntary Pension Insurance ACT | Amended | NO. 8/28.01.2003 |
| Insurance ACT | Amended | NO. 8/28.01.2003 |
| Public Offering of Securities ACT | Amended | NO. 8/28.01.2003 |
| Health Insurance ACT | Amended | NO. 8/28.01.2003 |
| Excise Duty ACT | Amended | NO. 9/31.01.2003 |
| Energy and Energy Efficiency ACT | Amended | NO. 9/31.01.2003 |
| ACT on the Mandatory Reserves of Oil And Oil Products | New | NO. 9/31.01.2003 |
| Competition Protection ACT | Amended | NO. 9/31.01.2003 |
| DECREE No. 16/30.01.2003 on the Execution of the 2003 State Budget | New | NO. 11/5.02.2003 |
| Cooperatives ACT | Amended | NO. 13/11.02.2003 |
| DECREE No. 18/4 February 2003 on Setting up a Coordination Council in Combating Delinquencies Affecting the Financial Interests of the European Community | New | NO. 13/11.02.2003 |
| DECREE No.21/4.02. 2003 on the Approval of International Accounting Standards Adopted by the International Accounting Standards Board | New | NO. 13/11.02.2003 |
| ORDINANCE on the Requirements to the Content of the Rationale on the Price of Shares in Public Companies Included for Assessment Methods Application, in the Cases of Transformation, Joint-Venture Contract and Commercial Offering | New | NO. 13/11.02.2003 |
| ORDINANCE on the Conditions to be Satisfied by Investment Projects Financed with State Loans and by Projects Applying for State Guarantee Finance, and on the Procedure of Their Consideration | New | NO. 15/14.02.2003 |
| Forestry ACT | Amended | NO. 16/18.02.2003 |
| ACT on 2003 State Budget of the Republic of Bulgaria. | Amended | NO. 16/18.02.2003 |
| ACT on Measures Against Financing of Terrorism | New | NO. 16/18.02.2003 |
| ACT on the 2003 Census of Farms in the Republic of Bulgaria. | New | NO. 17/21.02.2003 |
| DECREE No. 62 on Remitting the Act Amending the Privatization and Post-privatization Control Act to the National Assembly for Reconsideration, and Motives to the Decree | New | NO. 17/21.02.2003 |
| Consumer Protection and Trade Rules ACT (21.02.2003) | Amended | NO. 17/21.02.2003 |
| Patent LAW | Amended | NO. 17/21.02.2003 |
| DECREE No. 40/17 February 2003 on the Wage in Organizations and Activities Supported by the Budget | New | NO. 17/21.02.2003 |
| Technical Requirements to Products ACT | Amended | NO. 17/21.02.2003 |
| Health and Safety at Work ACT | Amended | NO. 18/25.02.2003 |
| COMMERCIAL CODE | Amended | NO. 19/28.02.2003 |
| Obligations and Contracts ACT | Amended | NO. 19/28.02.2003 |
| Special Pledges ACT | Amended | NO. 19/28.02.2003 |
| Consumer Protection and Trade Rules ACT | Amended | NO. 19/28.02.2003 |
| ORDINANCE No.2/7.01.2000 on Licenses and Permits Issued by the Bulgarian National Bank | Amended | NO. 19/28.02.2003 |
| ORDINANCE on the Procedure of Conducting Checks for Direct Control of the Protection of Classified Information | New | NO. 19/28.02.2003 |
| Structure of the Territory ACT | Amended | NO. 20/4.03.2003 |
| Seeds and Propagating Material ACT | New | NO. 20/4.03.2003 |
| Tobacco and Tobacco Products ACT | Amended | NO. 20/4.03.2003 |
| Privatization and Post-privatization Control ACT | Amended | NO. 20/4.03.2003 |
| DECISION No.117/21.02.2003 of the Council of Ministers on Approval of Annual List of Commercial Companies with State Interest in their Capital Offered for Privatization, for Which Payment by Non-monetary Payment Devices is Allowed in 2003 | New | NO. 20/4.03.2003 |
| ORDINANCE on the General Requirements to Guarantee Industrial Security | New | NO. 22/11.03.2003 |

ANNEX 2:REGULATORY DOCUMENTS PROMULGATED IN THE FIRST QUARTER OF 2003

| | | |
|--|---------|-------------------|
| DECISION of the National Assembly for Approval of Decision No. 147/2003 of the Council of Ministers for Appointing the Successful Tenderer in the Competition for Privatization of 5 893 778 Shares Representing 80 per cent of the Capital of Bulgartabac Holding AD, Sofia | New | NO. 24/14.03.2003 |
| ORDINANCE No. 5/2003 on the Procedure of Environmental Impact Assessment for National and Regional Development Plans and Programs, Structure Plans and Amendments Thereof | New | NO. 24/14.03.2003 |
| ORDINANCE on the Terms and Procedure of Conducting Environmental Impact Assessment for Investment Proposals for Construction, Activities, and Technologies | New | NO. 25/14.03.2003 |
| Employment Promotion ACT | Amended | NO. 26/21.03.2003 |
| ORDINANCE on the National Environment Management and Audit Scheme | New | NO. 26/21.03.2003 |
| ORDINANCE on the Terms and Procedure of Issuing Integrated Permits for the Construction and Use of New and for the Use of Operating Industrial Plants and Facilities | New | NO. 26/21.03.2003 |
| INSTRUCTION No. 1/2000 on Collecting Data from Insurers about the Insured Persons and from Self-Insured Persons | Amended | NO. 26/21.03.2003 |
| DECREE No. 307/27.12.1996 of the Council of Ministers on the Procedure for Coordination and Implementation of Republic of Bulgaria's Obligations as a World Trade Organization (WTO) Member | New | NO. 27/25.03.2003 |
| NATIONAL FRAMEWORK AGREEMENT between the National Health Insurance Fund, and the Bulgarian Doctors Union and the Union of Dentists in Bulgaria, 2003 | New | NO. 29/31.03.2003 |
| Bulgarian Identity Documents ACT | Amended | NO. 29/31.03.2003 |
| ORDINANCE on the Terms and Procedure of Issuing Integrated Permits for the Construction and Use of New and for the Use of Operating Industrial Plants and Facilities | Amended | NO. 29/31.03.2003 |

A. THE REVIEW OF BULGARIAN ECONOMY

The present review of Bulgarian economy is an authentic expert product of the Center for Economic Development, which was made possible mostly owing to the long experience of the Center in the field of applied studies of the economic policy and economic development of the country.

The review of Bulgarian economy in the first quarter of 2003 contains detailed presentation of this last period, assessment of the period and subsequent trends. The review is explicitly focused on this quarter of the current year. Where necessary, significant events, facts and data of periods prior to or after the end of the quarter have been highlighted. Where possible, two main types of data comparisons have been made: against the corresponding period of 2002 or against the previous quarter (end of 2002). Again where possible, the dynamics within the quarter itself has been traced, too. At many points also the short-term trend has been outlined.

The structure of the presentation above follows two principles simultaneously. First, the strive is towards giving a more comprehensive presentation of the subject matter areas, with corresponding prioritization of the range of matters discussed. Second, the different topics and analyses reflect the experience and interests of the experts and of the Center for Economic Development as a whole.

The review of Bulgaria's economy in the first quarter of 2003 starts with presentation of the findings of the business climate survey. The latest values of the Estat index of business climate in Bulgaria are presented. On the basis of the results of the survey an analysis is made of the condition and prospects of the business environment in our country. The business surveys conducted by NSI are presented immediately after that.

The overall dynamics of the economy in the first quarter of 2003 has been discussed against the background of the following basic categories: GDP, inflation, and labor market. The fiscal review of the quarter starts

with a presentation of the budget implementation. The fiscal review covers also the topics on foreign debt and domestic debt. The privatization topic is followed by the area of small and medium-sized enterprises. The foreign economic relations followed by foreign investments are presented in statistical terms and in their thematic relation, by means of data about the balance of payments and foreign trade. Then comes the review of a number of sectors of significant importance to the economic development of Bulgaria - energy, transport, high technologies, communications, tourism and agriculture. The financial sector is discussed by means of the capital market and the banking system. The wide topic of social policy and industrial relations encompasses the issues of social security, employment and unemployment, labor market policy, income and living standards, social assistance, and social partnership. The current problems and condition of the healthcare reform are discussed briefly. The environmental policy is considered simultaneously as a specific element of the economic policy and a factor for the economic environment. The specialized analysis of the process of Bulgaria's accession with the EU is underpinned by the understanding that in the course of these negotiations often the most determinative elements of economic policy are defined. There exists also a two-way interdependence between the competitiveness of the Bulgarian economy at macro- and company level, and the status of the negotiations. That is why in the context of the review and general analysis of the Bulgarian economy in the first quarter of 2003 the choice was made to lay down the emphasis on the negotiations for EU membership as the most significant aspect of the European integration process, which encompasses the adaptation and application of the *acquis*.

An integral part of the presentation is the annex containing the list of newly passed legislation and amendments to laws, which are of significant importance to the economic development of the country, and were promulgated in the Official Gazette in the first quarter of the year (Annex 2).

The work was finally completed on 9 June 2003.

B. SOURCES

Alongside with the conclusions from the large number of their own outputs and works, some of which are parts of concrete research projects, the experts of the Center for Economic Development have used statistical and other information and data from the following sources:

- National Assembly
- Council of Ministers
- Ministry of Energy and Energy Resources
- Ministry of Agriculture and Forestry
- Ministry of Economy
- Ministry of Regional Development and Public Works
- Ministry of Transport and Communications
- Ministry of Labor and Social Policy
- Ministry of Environment and Water
- Ministry of Finance
- National Statistical Institute
- National Social Security Institute
- Employment Agency
- Agency for Small and Medium-sized Enterprises
- Privatization Agency
- Bulgarian National Bank
- Bulgarian Stock Exchange - Sofia AD
- Financial Supervision Commission
- State Energy Regulatory Commission
- Delegation of the European Commission
- European Union
- International Energy Agency
- EUROSTAT
- Official Gazette

The particular sources and publications are quoted at the respective places in the text.

C. THE ESTAT INDEX OF BUSINESS CLIMATE IN BULGARIA

The business climate survey is based on own original methodology, developed by the team of the Agency for Social and Marketing Surveys Estat and the Center for Economic Development. The more

significant details are described below.

Methodology of the Sample

The survey was conducted in the period 2 - 11 April 2003 among the managers of 398 companies. The sample is a two-level panel one (at the first level the companies are divided into groups by regions, and at the second level - according to their economic sectors as per nomenclature A6 of the NSI), and it is grouped on the basis of the indices "number of employees" and "type of ownership". The sample is a guaranteed representative one at the level of going concerns.

Methodology of the Registration

The information has been collected using the method of an inquiry at the work place. The interviews were held with the owners of the companies covered by the sample, or with persons authorized to make management decisions and to sign financial statement documents (managers, chief accountants, commercial or marketing directors).

The questionnaire contains eight substantive questions and three passport questions. The integrated index is comprised of three components. The questions from one to five inclusive comprise Component I – "General Condition of the Company"; question six - Component II – "Investment Attitudes and Corporate Strategies"; questions seven and eight - Component III – "Business Environment".

General Description of the Index Calculation

1. Preliminary preparation

The preliminary preparation includes weighting of data according to the indices "economic sector" and "number of employees", recoding and calculating values for the respective questions.

- Questions with one possible answer

The original scales are of Likert type with codes from 1 (the highest degree) to 5 (the lowest degree). Recoding is done in such a way that the scale to

be from -2 (the lowest degree) to +2 (the highest degree).

- Multiple choice questions
These questions are recoded in advance in such a way that the possible answers are located symmetrically on both sides of the neutral point (the zero).

2. Calculation of the components

The index for each question (indicator) is calculated as a weighted average value.

Weights are assigned to each indicator within a component by means of expert evaluation. The value for each component (“General Condition of the Company”; “Investment Attitudes and Corporate Strategies”; “Business Environment”) is calculated as a weighted average.

The first table above shows the values obtained for the three components and the integrated index.

3. Calculation of an integrated index

The integrated index is calculated as a weighted average of the three components. The weight for each of the components is determined by means of expert evaluation.

The Estat index of business climate assumes values from -100 to +100. The business climate condition is assessed according to the following scale, similar to the one used in the German IFO Business Climate Index:

| | |
|-------------|-----------|
| -100 to -61 | very poor |
| -60 to -21 | poor |
| -20 to +20 | average |
| +21 to +60 | good |
| +61 to +100 | very good |

Interpretation

All components (with no exception), as well as the integrated index assume values within the interval [-100, +100]. The set of tools allows to determine also

the direction of the index. The difference between the values of questions Q3 (assessment of the expected condition), Q2 (assessment of the condition at a certain point in time) and Q1 (assessment of the condition during the preceding period) is applied as a criterion for determining the direction.

Beside everything aforesaid about the methodology, in many cases throughout the text additional methodological and other notes and comments are given.

CENTER FOR ECONOMIC DEVELOPMENT

1, Balsha Street, Block 9
Sofia 1408, BULGARIA
Telephone: 953 4204
Fax: 953 3644
e-mail: ced@ced.bg
www.ced.bg